Supreme Court
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ALEXANDER L. STEVAS,
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No. 80-1252

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

COMMONWEALTH OF PUERTO RICO,
Petitioner,

v.

DONALD T. REGAN, SECRETARY,
DEPARTMENT OF THE TREASURY,
Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The District of Columbia Circuit

PETITION FOR CERTIORARI

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QUESTIONS PRESENTED

1. Whether the plain language of 48 U.S.C. §734 that "all taxes collected under the internal revenue laws of the United States on articles produced in Puerto Rico and transported to the United States, or consumed in the island shall be covered into the Treasury of Puerto Rico" compels the covering over to the treasury of Puerto Rico of federal excise taxes collected on gasoline produced in Puerto Rico and transported to the United States.

2. Whether the gasoline excise tax imposed by 26 U.S.C. §4081 is a tax on manufacture and hence legally indistinguishable from the excise taxes imposed on liquor and tobacco products by 26 U.S.C. §§5001 and 5701.*

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* Similar questions are presented by the petition for certiorari which is being filed by the Virgin Islands. Those questions were presented to, and decided by, the United States Court of Appeals for the District of Columbia in Case No. 79-1021 with respect to gasoline refined in the Virgin Islands and transported to the United States. The portion of No. 79-1021 dealing with the gasoline excise tax issues was addressed by the Court of Appeals in its opinion in the Puerto Rico case, No. 79-1020.

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On Writ Of Certiorari To The United States Court Of Appeals For The District of Columbia Circuit

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PETITION FOR CERTIORARI

Petitioner Commonwealth of Puerto Rico prays that a writ of *certiorari* issue to review the judgment and opinion of the United States Court of Appeals for the District of Columbia Circuit.[1]

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[1] W. Michael Blumenthal, Secretary of the Treasury, was Defendant—Appellant—Cross-Appellee below. Mr. Blumenthal has ceased to hold office, and pursuant to Rule 40.3, the present secretary is substituted automatically as respondent.

OPINIONS BELOW

The opinion of the Court of Appeals, not yet officially reported, is reproduced as Appendix A to this petition. The opinion of the United States District Court for the District of Columbia is not reported and is reproduced as Appendix B to this petition.

JURISDICTION

The judgment of the United States Court of Appeals for the District of Columbia Circuit was entered on October 17, 1980. A timely Petition for Rehearing and Suggestion for Rehearing *En Banc* was filed, and by separate orders dated December 18, 1980 (copies reproduced as Appendices C and D), the Court of Appeals denied rehearing and rehearing *en banc*. This petition for *certiorari* is filed within ninety days of that time.[2] This Court's jurisdiction is invoked under 28 U.S.C. §1254(1).

STATUTES INVOLVED

This case involves the effect of 48 U.S.C. §734, which reads in pertinent part:

> "[A]ll taxes collected under the internal revenue laws of the United States on articles produced in Puerto Rico and transported to the United States, or consumed in the island shall be covered into the Treasury of Puerto Rico."[3]

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[2] On December 23, 1980, petitioner moved, in accordance with Fed.R.App.P. 41(b), to stay the issuance of the Court of Appeals mandate to and including January 26, 1981. That motion has not yet been acted upon.

[3] This statutory provision also is codified as section 7652(a)(3) of the Internal Revenue Code, 26 U.S.C. §7652(a)(3).

The case also involves the provisions of 26 U.S.C. §§4081-4083, 5001, 5006, 5701-5703, 7652(a)(1) & (3) and 31 U.S.C. §725s[b](62), the pertinent portions of which are reproduced as Appendix E.

STATEMENT OF THE CASE

Section 734 of Title 48 U.S.C. provides that "all taxes collected under the internal revenue laws of the United States on articles produced in Puerto Rico and transported to the United States, or consumed in the island shall be covered into the Treasury of Puerto Rico." Pursuant to that statute respondent and his predecessors consistently have covered into the treasury of Puerto Rico all United States internal revenue taxes collected on liquor and tobacco products produced in Puerto Rico and transported to the United States.

Since approximately July 1, 1956, and continuing on a current basis, gasoline has been refined in Puerto Rico and transported to the United States. Throughout that period, upon sale in this country by the manufacturer or importer, such gasoline has been subjected to the United States internal revenue tax imposed by 26 U.S.C. §4081, and taxes have been collected on such gasoline. However, respondent has refused, and continues to refuse, to cover over such taxes to the treasury of Puerto Rico.

As a result of that refusal, and having exhausted all available administrative remedies, on June 26, 1975 petitioners commenced an action in the United States District Court for the District of Columbia against the Secretary of the Treasury for declaratory and injunctive relief and mandamus requiring him to comply with the terms of the statute. The District Court had jurisdiction pursuant to 28 U.S.C. §§1331, 1340, 1361, & 2201. In

an unreported decision filed October 10, 1978, the District Court (Judge Oliver Gasch) upheld Puerto Rico's position on the meaning of section 734 and ordered that the gasoline taxes in question be covered into the treasury of Puerto Rico, but restricted its recovery of past collections by application of a laches theory. (58a, *infra*). Respondent appealed the District Court's ruling on the merits; Puerto Rico cross-appealed the District Court's laches holding.

By decision dated October 17, 1980, a panel of the Court of Appeals (Circuit Judges McGowan and Wald and District Judge Pratt, sitting by designation) reversed the District Court, concluding that the statute requires the covering over only of so-called equalization taxes (such as the liquor and tobacco taxes) imposed by the Foraker Act, 26 U.S.C. §7652(a)(1) (39a, *infra*), and that the gasoline excise tax is not such a tax (39a, *infra*). The Court of Appeals did not reach the laches issue. On October 31, 1980, Puerto Rico filed a timely Petition for Rehearing and Suggestion for Rehearing *En Banc*. By separate orders dated December 18, 1980 rehearing and rehearing *en banc* were denied.

REASONS FOR GRANTING THE WRIT

This case, involving more than a billion dollars, vitally affects the fiscal and political relationships between the United States and the governments of the Commonwealth of Puerto Rico and the Territory of the Virgin Islands. The Court of Appeals held in effect that the term "all taxes" really means only "some taxes"; that a Senate Report explicitly stating a legislative intent to make the covering over provision "all-inclusive" in fact evidenced a Congressional purpose to limit that provision to certain "equalization taxes"; that a small

group of largely secret internal documents, carefully selected by respondent, evidenced a consistent course of administrative construction; and that a tax which this Court has held is laid on manufacturers of gasoline is not a tax on manufacturing. In so holding the lower Court created a loophole in the tax laws that will permit certain gasoline coming into this country from Puerto Rico to escape taxation altogether and departed irreconcilably from this Court's prior holding that a tax laid on tobacco "manufactured in or imported into the United States and hereafter *sold by the manufacturer or importer*" (emphasis supplied) is a tax on manufacture. These circumstances require the exercise of this Court's *certiorari* jurisdiction, as we show in more detail below.

I. As The Government Has Conceded, This Case Presents Significant Issues Of Historic Importance Concerning The Fiscal Relationship Between The Federal Government And The Governments Of Puerto Rico And The Virgin Islands.

The importance of the issues at bar is emphasized by the fact that respondent, the Secretary of the Treasury, sought a hearing *en banc* by the Court of Appeals in the first instance. The Suggestion by the Secretary of the Treasury For Hearing En Banc (Appendix F) followed the entry of an order by the motions panel of the Court of Appeals (Judges Bazelon, Tamm and Robinson) denying respondent's motion for a stay of the District Court's decision and requiring the establishment of an interest-bearing escrow account to

hold the revenues at issue pending appeal.[4] In his suggestion for hearing *en banc*, respondent stated:

> "The instant appeals involve issues of exceptional importance to the United States of America, the Commonwealth of Puerto Rico and the Virgin Islands. We have been informed by the Assistant General Counsel, Department of the Treasury, that the substantive issues involve approximately one billion dollars. Additional millions are being added to this amount each month." *Id.* (69a, *infra*).

Elsewhere in that pleading respondent refers to the issues as "extremely important" and of "exceptional importance". *Id.* (70a, 71a, *infra*). Petitioner endorses the Secretary's view of the importance of these issues. The record indicates that, through 1974, over $350 million is at issue in the Puerto Rico case, and preliminary estimates indicate that the sum is increasing at a rate of approximately $20 million per year.

The sheer numbers of dollars involved are, however, only part of the importance of this case. Since passage of the "Jones Act" of 1917, 39 Stat. 951, the return of U.S. taxes collected on Puerto Rican products has been both the principal form of direct United States support for the territorial (and later, Commonwealth) government of Puerto Rico and a very significant source of funding for that government.[5] Indeed, it has been

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[4] In accordance with the motion panel's February 12, 1979 Order (Judge Robinson not participating), from October 10, 1978 (the date of the District Court's decision) through July 1, 1980 (the last date for which Puerto Rico has been supplied figures), approximately $38.7 million have been deposited in a special account established by the Secretary to hold the funds at issue in the Puerto Rico case. A similar account also has been established for the Virgin Islands. Interest continues to accumulate on those funds, which in turn is deposited in the special accounts.

[5] The tax revenues at issue are critically needed by the Commonwealth of Puerto Rico, whose citizens have a lower per capita income than the citizens of any State in the Union.

suggested by federal officials that the covering over procedure is a substitute for the federal revenue sharing program, from which Puerto Rico is excluded. So important is the covering over provision that it was expressly included in The Puerto Rican Federal Relations Act of 1950, Pub.L. No. 600, 64 Stat. 319, as one of the terms of the Compact between the United States and Puerto Rico.[6] The decision below profoundly affects the scope of the covering over provision, thus striking at the heart of the fiscal relationship between the United States and Puerto Rico[7] and altering a key element in the fundamental political relationship between the two governments.

The undisputed importance of the case to the three governments involved, the enormity of the sums at issue, and the novel questions presented concerning the fiscal relationships between the Federal Government and the governments of Puerto Rico and the Virgin Islands, fully warrant the Court's consideration of this case.

II. The Decision Below Conflicts Irreconcilably With The Principle Of Statutory Construction Enunciated By This Court In *TVA* v. *HILL*.

As indicated above, 48 U.S.C. §734 provides that

> "all taxes collected under the internal revenue laws of the United States on articles produced in Puerto Rico and transported to the United States, or con-

[6] Courts have stated that the provisions of the Compact cannot be unilaterally changed either by the United States or by Puerto Rico. United States v. Valentine, 288 F. Supp. 957, 981 (D.P.R. 1968); Mora v. Torres, 113 F. Supp. 309, 313 (D.P.R. 1953); *see* Calero-Toledo v. Pearson Yacht Leasing Co., 416 U.S. 663, 671-673 (1974).

[7] The decision below has a similar disruptive effect on the fiscal relationship between the United States and the Virgin Islands.

> sumed in the island shall be covered into the Treasury of Puerto Rico."

Notwithstanding the clear statutory admonition that "all taxes" on Puerto Rican articles coming into the United States be covered over, the Court of Appeals viewed the language as "highly ambiguous" (11a, *infra*); then, based on a contorted analysis of the legislative history and a highly selective review of the administrative construction, it accepted respondent's argument that only some, but not "all", taxes imposed under the internal revenue laws of the United States on articles produced in Puerto Rico and transported to the United States should be covered into the treasury of Puerto Rico.

The Court of Appeals thus contravened the seminal principle frequently enunciated by this Court[8] that, when a statute is clear on its face, there is no need to resort to its legislative history, its administrative construction, or other aids to statutory interpretation. That principle is made especially clear in *TVA* v. *Hill*, 437 U.S. 153 (1978), where the Court, relying on the plain meaning of the Endangered Species Act, upheld an injunction forbidding impoundment of water in the virtually completed Tellico Dam because the operation of that dam would eradicate a small fish called the snail darter, an endangered species. *Id.* at 184, n. 29. The principle has been held to override even the policy of deference to an agency's interpretation:

> "[T]he sound principle of according deference to administrative practice normally applies only where

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[8] *See, e.g.*, Packard Motor Car Co. v. NLRB, 330 U.S. 485, 492 (1947); Kuehner v. Irving Trust Co., 299 U.S. 445, 449 (1937); Fairport, P. & E. R.R. v. Meredith, 292 U.S. 589, 594-595 (1934); Wilbur v. United States ex rel. Vindicator Consol. Gold Mining Co., 284 U.S. 231, 237 (1931).

> the relevant statutory language is unclear or susceptible of differing interpretations." *Shea* v. *Vialpando*, 416 U.S. 251, 262, n.11 (1974).

See also Townsend v. *Swank*, 404 U.S. 282, 286 (1971).

A. Legislative history

Contrary to the lower court's interpretation, the legislative history of the covering over provision is devoid of any expression of intent to limit that provision to equalization taxes. On the contrary, the legislative history conclusively demonstrates that *all* taxes on articles produced in Puerto Rico and transported to the United States are to be covered over to Puerto Rico.

The House Report cites two reasons for enactment of the covering over provision. First, the Report evidenced concern about the financial embarrassment to the Puerto Rican government resulting from a $750,000 per year decline in revenues from customs duties. H.R. Rep. No. 77, 64th Cong., 1st Sess. 1-2 (1916). Since the amount of Foraker taxes collected in 1916 was only about $500,000 per year, it seems obvious that there could have been no intent to limit the covering over provision to a sum only two-thirds as large as the deficit at which it was directed.[9] Second, the House Report stated:

> "It is believed to be but just and fair that it [Puerto Rico] should receive the internal revenue taxes collected upon its products, whether those products are used in Puerto Rico or produced in Puerto Rico and transported to and used in the United States." *Id.*

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[9] In any event, the broader purpose of alleviating financial embarrassment obviously would be better served by an expansive covering over provision than by one limited to equalization taxes.

Clearly the interests of fairness and justice, which were thought to require rebate to Puerto Rico of all taxes collected under United States internal revenue laws on Puerto Rican products, would not be satisfied by the covering over of only some such taxes.

That Congress did not intend to limit the covering over provision to equalization taxes is conclusively demonstrated by the action of the Senate. That body amended the House bill to ensure that the covering over provision included taxes on articles produced "elsewhere" (not just in the United States) but consumed in Puerto Rico. The Committee explained the purpose of its amendment in the following language:

> "The purpose of the above amendments is to make clear the intent that *all money collected on account of internal revenue shall accrue to the government of the island*, applying as well to articles *produced elsewhere* but consumed in the island. *With these amendments the provision relating to disposition of internal revenue becomes all inclusive, which is the intent.*" S. Rep. No. 579, 64th Cong., 1st Sess. 2 (1916) (emphasis supplied).

Thus, the Senate clearly expressed its intent to make the covering over provision "all inclusive"; it did not, as it could easily have done, attempt to limit the provision to equalization taxes, or even to taxes on products produced in the United States (which might be subject to equalization taxes if consumed in Puerto Rico).[10]

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[10] The Court's attempt to explain the Senate amendment by stating that "Congress made the cover over provision perfectly coextensive with the Foraker equalization tax" (21a, *infra*) by "merely extend[ing] the cover over provision to the only remaining portion of Foraker equalization taxes not yet included in the cover over provision . . ." (22a, *infra*), does not withstand analysis, because it does not explain, and in fact is refuted by, the phrase "produced elsewhere" in the Senate Report. By providing for the

B. Administrative construction

The Court of Appeals also purported to find support for its decision in respondent's administrative constructions of the statute, which the Court stated were entitled to great weight because they are "both consistent and public." (28a, *infra*). They are neither.

Of the four "major administrative constructions" upon which the panel's decision relies, *id.*, two are found in non-public Internal Revenue Service documents that were obtained through discovery in this proceeding.[11] Because those documents (including one that respondent described as "of most immediate relevance to this case") were not publicly available, it was improper for the Court of Appeals to give weight to the fact that "Puerto Rico has never challenged this interpretation nor Congress amended the statute to override this interpretation." (28a, *infra*).

More important, however, it is fundamentally unfair and improper for respondent (and the Court of Appeals) to draw any inference from a "consistent" course of administrative construction when respondent alone has decided which administrative constructions shall be put in the record. Respondent withheld (on grounds of privilege) twenty-three concededly relevant documents, many of which appear from their descriptions to bear importantly on the administrative construction

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covering over of taxes on articles produced elsewhere but consumed in the island, the Senate clearly provided for the possibility that such articles could originate in foreign countries as well as in the United States. Such foreign articles obviously would not be subject to equalization taxes.

[11] A third, Revenue Ruling 58-554, 1958-2 Cum.Bull. 909, which the Court states is "on all fours with . . . [its] view" (32a *infra*), does not even mention the covering over provision.

question.[12] His refusal to produce all administrative construction documents, and the Court's acquiesence in that refusal, unfairly deprived petitioner of any meaningful opportunity to rebut the construction argument.[13] *Cf. Illinois State Employees Union* v. *Lewis*, 473 F.2d 561, 565-566 (7th Cir. 1972), *cert. denied*, 410 U.S. 928 (1973); *Washington* v. *Cameron*, 411 F.2d 705, 710-711 (D.C. Cir. 1969).

In short, the plain language of the statute requires that all U.S. taxes collected on Puerto Rican articles coming to the United States be covered over to Puerto Rico. The lower court's holding to the contrary is thus inconsistent with this Court's decision in *TVA* v. *Hill*. In these circumstances, the Court should exercise its discretionary review power to rectify a clear and important departure from its precedents.

III. The Decision Below Would Hamper Proper Administration Of The Gasoline Excise Tax By Allowing Puerto Rican Gasoline To Escape Taxation And Is In Conflict With This Court's Decisions In *Liggett & Myers Tobacco Co.* v. *United States* And *Gurley* v. *Rhoden*.

The lower court's unjustifiably narrow interpretation of the covering over provision was the predicate for its further holding that the gasoline tax is not a manufacturing tax and thus not an equalization tax that

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[12] Petitioner's motion to compel production of the twenty-three documents was denied without opinion by the District Court.

[13] A number of documents that were not produced appear to suggest a contrary interpretation. For example, one document obtained through discovery refers to another document (which was not porduced) suggesting that " §3360(c) of the Code [the covering over provision] as to Puerto Rico [is] so broad as to include any Federal tax collected at any time on articles which have an origin in . . . Puerto Rico."

can be imposed on Puerto Rican articles through the Foraker taxing provision. The second branch of the opinion below has even more serious implications for the proper administration of the gasoline tax and is in fundamental conflict with two prior decisions of this Court.

A. The lower court's decision would allow gasoline refined in Puerto Rico and transported to the United States to escape taxation.

In attempting to distinguish the liquor and tobacco taxes from the gasoline excise tax, respondent continually has asserted, without any support, that the taxes imposed on liquor and tobacco products manufactured in Puerto Rico and shipped to the mainland are equalization taxes necessarily imposed by the Foraker Act, 26 U.S.C. §7652(a)(1), while the tax on gasoline is not an equalization tax imposed by the Foraker Act but rather is imposed directly by 26 U.S.C. §4081(a). The Court of Appeals adopted that position. (35a-36a, *infra*).

Sections 5001 and 5701 of Title 26 impose taxes on liquor and tobacco products manufactured in or imported into the United States.[14] The only conceivable reason that those sections would not reach shipments of liquor or tobacco products from Puerto Rico is that such shipments are not considered imports. Indeed, documents obtained by petitioner through discovery in this action appear to confirm that as respondent's established interpretation.

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[14] Section 5001 imposes a tax on "all distilled spirits in bond or produced in or *imported into* the United States", and section 5701 imposes a tax on tobacco products manufactured or *imported into* the United States". (63a, 64a, *infra*) (emphasis supplied).

By accepting respondent's argument, however, the Court of Appeals reached an anomalous and erroneous result. If such shipments are *not* imports, then persons who transport gasoline from Puerto Rico for sale in the United States cannot be taxed as importers under section 4081(a).[15] Thus, under the Court's interpretation, gasoline sold by a Puerto Rican "importer" (other than a manufacturer) directly to a retailer in the United States must be taxed under the Foraker Act, lest the gasoline escape taxation altogether.[16] Therefore, the equalization provision of the Foraker Act would be necessary to impose a tax on some gasoline shipped from Puerto Rico to the United States, just as the Foraker Act is concededly necessary to impose a tax on liquor and tobacco coming to this country from the Commonwealth.

By concluding that the gasoline tax is *not* an equalization tax, (*i.e.*, not one that can be imposed by the Foraker taxing provision) the decision below thus makes it possible for some Puerto Rican gasoline to avoid all taxation. Such a result clearly was not intended by Congress. It was precisely this analysis that led the District Court to determine that "the illogic of defendant's asserted distinction" merely demonstrates "the weakness of defendant's construction of the cover over provision." (53a, *infra*). Indeed, as the District Court also noted, defendant's argument "has proven too much (54a *infra*), for it demonstrates the equivalency of all three taxes.

[15] Section 4081 imposes a tax on gasoline sold by the "manufacturer or importer thereof."

[16] Indeed, documents obtained through discovery recognize this possibility. *E.g.*, one document notes: "[I]f goods that are brought into this country from Puerto Rico are not imports . . . [shippers] might escape taxes completely."

B. The gasoline excise tax is a manufacturing tax.

The Court of Appeals ruled that the gasoline excise tax is not an equalization tax because, unlike the liquor and tobacco taxes, it is a "tax on *sale*". (35a, *infra*) (emphasis in original). The Court's holding is in conflict with the legislative history of the gasoline excise tax, defendant's own administrative construction, and this Court's decisions in *Liggett & Myers Tobacco Co.* v. *United States*, 299 U.S. 383 (1937), and *Gurley* v. *Rhoden*, 421 U.S. 200 (1975).

The legislative history of the gasoline excise tax could hardly be clearer; the tax is laid on the *article*. In the Senate debate on the Revenue Act of 1932, which first imposed the present tax, Senator Walsh stated:

> "The manufacturers' excise tax proposal is to lev [sic] the tax once, *upon the article, in its finished state. . . .*" 75 Cong. Rec. 11657 (1932) (emphasis supplied).

See also Remarks of Congressman Mills in connection with the Highway Revenue Act of 1956, 70 Stat. 387, 102 Cong. Rec. 7159 (1956) ("[t]he *existing tax on gasoline is a manufacturer's tax* imposed at the time of sale by the manufacturer") (emphasis supplied).

The Court's decision that the gasoline tax is a sales tax is further undercut by respondent's own administrative construction. Prior to its repeal in 1950, section 2301 of the Internal Revenue Code of 1939 imposed a one-quarter cent per pound tax on oleomargarine "*manufactured and sold*, or removed for consumption or sale" (emphasis supplied), language quite similar to that found in the gasoline tax ("sold by

the manufacturer"). Respondent has admitted that: "The tax on margarine was considered [by the Internal Revenue Service] to be a tax on the *manufacture* of margarine rather than on its sale." Indeed, one of the documents disclosed in the course of discovery quite properly recognized that the Foraker taxing provision would have imposed this tax on oleomargarine manufactured in Puerto Rico and shipped to the United States.

Respondent's position on the margarine tax was no accident; it was required by the decision of this Court in *Liggett & Myers Tobacco Co.* v. *United States*, *supra*, a case which the Court of Appeals simply ignored. There the Court was asked to construe a predecessor of the current tobacco tax. The tax was laid—in language indistinguishable from that of the gasoline tax—"upon all tobacco and snuff manufactured in or imported into the United States, and hereafter *sold by the manufacturer or importer*, or removed for consumption or sale" (emphasis supplied). Applicable Treasury regulations prescribed that "[t]he tax accrues on such manufactures upon removal from the factory or place where they are made, *or upon sale prior to such removal.*" 299 U.S. at 384 (emphasis supplied). Petitioners alleged that the tax was a sales tax, but the government argued that it was a tax upon the manufacture of tobacco with the duty of payment postponed until removal or sale. *Id.* at 386. The Court squarely held that the levy was "an excise on manufacture", *id.* at 387, noting in support of that conclusion that the tax was laid upon each pound of tobacco manufactured, "irrespective of intrinsic value or price obtained upon sale," *id.* at 386. It recognized that "the limit of time for making payment is when the product is sold or removed", but explained that "this is a privilege designed to mitigate the burden." *Id.* The Court of Appeals decision squarely conflicts with the *Liggett & Myers* holding.

The decision below also is in conflict with this Court's recent unanimous decision in *Gurley* v. *Rhoden*, *supra*, concerning the very tax here at issue. *Gurley* confirms that the incidence of the gasoline excise tax is on the manufacturer or producer and not upon the consumer. 421 U.S. at 207-208. Thus, the case makes clear that the gasoline excise tax, like the excise taxes on alcohol and tobacco products, is a tax on manufacture or production; it is not a retail *sales* tax. The Court explicitly stated that the gasoline tax "attaches prior to the point of the retail sale." *Id.* at 211.

The mere inclusion of the word "sold" in a taxing statute does not prevent it from being a manufacturing tax or from being covered into the treasury of Puerto Rico. The decision of the Court of Appeals to the contrary is in conflict with legislative history, administrative construction, Supreme Court precedent, and common sense. This Court should grant *certiorari* to safeguard the integrity of its *Liggett & Myers* and *Gurley* holdings and to assure that the gasoline tax will apply to all gasoline manufactured in or transported into the United States.

CONCLUSION

For the reasons set forth above, a writ of *certiorari* should issue to review the judgment and opinion of the United States Court of Appeals for the District of Columbia Circuit.

Respectfully submitted,

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January 23, 1980

Certificate Of Service

I, Michael J. Henke, attorney for petitioner and a member of the Bar of this Court, certify that on this 23d day of January, 1981, the foregoing Petition for Certiorari has been served upon defendant by hand-delivering three copies thereof to David English Carmack, Department of Justice, Washington, D.C., attorney for defendant and by mailing three copies certified mail, postage prepaid, return receipt requested, to the Solicitor General, Department of Justice, Washington, D.C. 20530. I further certify that all parties required to be served have been served.

MICHAEL J. HENKE

APPENDIX

APPENDIX A

Notice: This opinion is subject to formal revision before publication in the Federal Reporter or U.S.App.D.C. Reports. Users are requested to notify the Clerk of any formal errors in order that corrections may be made before the bound volumes go to press.

United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 79-1020

COMMONWEALTH OF PUERTO RICO

v.

W. MICHAEL BLUMENTHAL, Secretary, Department of the Treasury, APPELLANT

No. 79-1021*

VIRGIN ISLANDS

v.

W. MICHAEL BLUMENTHAL, Secretary, Department of the Treasury, APPELLANT

No. 79-1024

COMMONWEALTH OF PUERTO RICO, APPELLANT

v.

W. MICHAEL BLUMENTHAL, Secretary, Department of the Treasury

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*In this opinion, we address that portion of No. 79-1021 dealing with the covering over of revenues derived from the taxation of gasoline refined in the Virgin Islands and transported to the United States. In a companion opinion issued simultaneously herewith, we dispose of another portion of No. 79-1021, the customs duties issue unique to the Virgin Islands case.

Bills of costs must be filed within 14 days after entry of judgment. The court looks with disfavor upon motions to file bills of costs out of time.

Appeals from the United States District Court
for the District of Columbia

(D.C. Civil Action Nos. 75-1035 & 76-0916)

Argued November 16, 1979

Decided October 17, 1980

Ernest J. Brown, Attorney, Department of Justice, with whom *M. Carr Ferguson*, Assistant Attorney General, and *David English Carmack*, Attorney, Department of Justice, were on the brief for the Secretary of the Treasury as appellant.

Michael J. Henke, with whom *Charles D. Tetrault*, was on the brief for the Commonwealth of Puerto Rico as appellee and cross-appellant.

Milton Eisenberg, with whom *Theodore C. Hirt* and *Ive Arlington Swan*, were on the brief for the Virgin Islands as appellee in case No. 79-1021.

Myron C. Baum also entered an appearance for the Department of Justice.

Before McGOWAN and WALD, *Circuit Judges*, and JOHN PRATT,** *United States District Judge* for the District of Columbia.

Opinion for the court filed by *Circuit Judge* McGOWAN.

McGOWAN, *Circuit Judge*: These consolidated appeals present a substantial controversy between the United States, on the one hand, and Puerto Rico and the Virgin Islands, on the other, with respect to the proper disposition of revenues derived from a tax of 4 cents per gallon imposed by the United States on the initial sale of gasoline in the United States by a producer or importer. 26 U.S.C.

** Sitting by designation pursuant to Title 28 U.S.C. § 292(a).

§ 4081(a) (1976). Each of the island governments asserts that Congress has directed that such revenues in respect of gasoline manufactured in the islands and transported to the United States should be paid over to them. The District Court upheld that contention. We reverse.

I

In 1898, the United States acquired Puerto Rico from the government of Spain pursuant to the Treaty of Paris, which ended the Spanish-American War. Treaty of Paris, Apr. 11, 1899, United States-Spain, 30 Stat. 1754. Soon after, Congress enacted the Foraker Act, also called the First Organic Act, 31 Stat. 77 (1900), which set up a provisional domestic government in Puerto Rico and provided revenues for the island's support. H.R. Rep. No. 249, 56th Cong., 1st Sess. 1–16 (1900). In order to aid the growth of Puerto Rican industries and professions, Congress provided in section 14 of the Foraker Act that "the internal revenue laws . . . in view of the provisions of section three, shall not have force and effect in Porto Rico." Foraker Act, § 14, 31 Stat. 77, 80 (1900). In section 3, however, Congress limited this exemption by subjecting articles manufactured in Puerto Rico and shipped to the United States to a permanent tax "equal to the internal revenue tax imposed in the United States upon the like articles of merchandise of domestic manufacture." Foraker Act, § 3, 31 Stat. 77 (1900). The Act did not mandate any special treatment of these tax revenues, and all were retained by the United States Treasury.

In 1917, Congress passed the Second Organic Act *eo nomine* the Jones Act, 39 Stat. 951 (1917), which provided, *inter alia*, "[t]hat hereafter all taxes collected under the internal revenue laws of the United States on articles produced in Porto Rico and transported to the United States, or consumed in the island *shall be covered into the treasury of Porto Rico.*" Jones Act, § 9, 39 Stat. 951 (current version at 26 U.S.C. § 7652(a)(3) (1976)) (em-

phasis added).[1] This cover over provision was enacted as part of the Puerto Rican Federal Relations Act of 1950, Pub. L. No. 600, 64 Stat. 319 (48 U.S.C. § 734), and is also codified at 26 U.S.C. § 7652(a)(3) (1976), the tax statute upon which Puerto Rico bases its claim.

Since the passage of the Jones Act, the United States Treasury has consistently covered over into the treasury of Puerto Rico revenues from manufacturer's excise taxes on liquor and tobacco produced in Puerto Rico and transported to the United States. During 1977 alone the revenues covered over totaled approximately $9 million in tobacco tax revenues and $134 million in liquor tax revenues (App. 297–98).

During fiscal year 1956–57 Puerto Rican manufacturers began to refine and ship gasoline to the United States. Upon sale, this gasoline was subject to a tax that has been levied since 1932 on all gasoline "sold by a producer or importer" in the United States. Revenue Act of 1932, § 617, 47 Stat. 169 (1932) (current version at 26 U.S.C. § 4081(a) (1976)). None of the revenues derived from gasoline manufactured in Puerto Rico and shipped to the United States have ever been covered over to Puerto Rico. The Secretary of the Treasury estimates that approximately $350,000,000 in tax revenues have been collected on Puerto Rican gasoline since 1956 (App. 213).

On September 13, 1974, the Governor of Puerto Rico wrote to the Secretary of the Treasury, requesting that both past and future tax revenues on gasoline produced in Puerto Rico and transported to the United States be cov-

[1] The spelling was then "Porto Rico." It was changed to "Puerto Rico" by the Joint Resolution of May 17, 1932, 47 Stat. 158 (1932). The phrase "covered into" means, literally, "deposited into." In practical terms, the provision requires the United States to rebate to the Puerto Rican treasury the same amount of funds as it collected through taxation of Puerto Rican articles in the above-described circumstances.

ered over into the treasury of Puerto Rico (App. 15). After exchanging letters and legal memoranda regarding the cover over provision, the parties could not agree, and the Secretary formally rejected Puerto Rico's claim on June 10, 1975 (App. 59).

Puerto Rico brought suit in the District Court, seeking declaratory relief, mandamus, an injunction against future retention of the gasoline tax revenues, and an accounting of all sums unlawfully withheld in the past. *Commonwealth of Puerto Rico v. Blumenthal*, No. 75–1035 (D.D.C. Oct. 10, 1978). On October 10, 1978, the District Court granted partial summary judgment. The court held that Puerto Rico is entitled to all tax revenues henceforth collected on gasoline manufactured in Puerto Rico and transported to the United States, but limited Puerto Rico's recovery of the past tax revenues to those collected after September 13, 1974, when Puerto Rico first informed the Secretary of the Treasury of its claim. *Id.* at 15–18. The court reasoned that Puerto Rico had "slept on its rights" and therefore was barred from full recovery by the equitable doctrine of laches.[2]

The facts of the Virgin Islands case are essentially the same. The Virgin Islands were acquired from Denmark pursuant to the Treaty of August 4, 1916, United States-Denmark, 39 Stat. 1706. On March 3, 1917, Congress passed an act providing for government of the Virgin Islands. Act of March 3, 1917, 39 Stat. 1132 (1917). Included was a tax provision analogous to section 3 of the Foraker Act. In its current form, the Virgin Islands equalization tax statute provides in pertinent part:

> *Taxes imposed in the United States.* — Except as provided in section 5314, there shall be imposed in the

[2] In Nos. 79–1020 & 1021, the United States appeals the District Court's grant of partial summary judgment. In No. 79–1024, Puerto Rico cross-appeals the District Court's application of the doctrine of laches to prevent Puerto Rico's recovery of all taxes ever levied on Puerto Rican gasoline.

> United States, upon articles coming into the United States from the Virgin Islands, a tax equal to the internal revenue tax imposed in the United States upon like articles of domestic manufacture.

26 U.S.C. § 7652(b)(1) (1976). The Internal Revenue code now provides for cover over of a certain percentage of

> all taxes imposed by, and collected during the fiscal year under, the internal revenue laws of the United States on articles produced in the Virgin Islands and transported to the United States.

26 U.S.C. § 7652(b)(3) (1976).

In 1966, the Virgin Islands began to refine gasoline for sale in the United States. All such gasoline sold in the United States was taxed pursuant to the same gasoline tax, 26 U.S.C. § 4081(a) (1976), at issue in the Puerto Rico case. The United States Treasury neither covered over these funds nor set up a special fund for the benefit of the Virgin Islands. The Virgin Islands sued seeking, among other relief, (1) a declaratory judgment that the gasoline excise tax revenues collected by the Treasury since 1966 should be covered into the treasury of the Virgin Islands, and (2) payment of all future taxes and all past taxes wrongfully withheld. *Virgin Islands v. Blumenthal*, No. 76-0916 (D.D.C. Oct. 11, 1978). The District Court granted the Virgin Islands' motion for summary judgment.

Four appeals in all were consolidated for hearing and disposition. Nos. 79-1020 & 1024 are the cross-appeals involving the gasoline tax issue with respect to Puerto Rico. Nos. 79-1021 & 1022 are the cross-appeals involving both the gasoline tax and customs duties issues with respect to the Virgin Islands.

This opinion deals with the gasoline tax questions as to both Puerto Rico and the Virgin Islands. A companion opinion issued simultaneously herewith disposes of the customs duties problems which are confined to the Virgin Islands. We consider the gasoline tax questions together because the cover over statute upon which the Virgin Is-

lands rely is in all essential aspects identical to that of Puerto Rico, and almost certainly was consciously patterned after the Puerto Rico provision. *See* S. Rep. No. 1271, 83rd Cong., 2d Sess. 4 (1954); S. Rep. No. 476, 80th Cong., 1st Sess. 2-3 (1947). The District Court, as well as the parties themselves, focused on the Puerto Rico cover over provision throughout the litigation and assumed that an interpretation of the meaning of the Puerto Rico cover over provision determines the meaning of the other provision as well. *Virgin Islands v. Blumenthal*, No. 76-0916 (D.D.C. Oct. 11, 1978), slip op. at 2. We adopt this approach, and assume that an interpretation of the Puerto Rico statute is applicable to the Virgin Islands statute as well.

II

The District Court held that the cover over provision by its terms is all-inclusive and should be interpreted broadly, not limited only to Foraker Act taxes. The court read the cover over provision to require the covering over to Puerto Rico of all taxes on all articles produced in Puerto Rico and transported to the United States, without regard to which statutory provision imposes the tax. But, the court found further, even under the narrower view of the cover over provision espoused by the United States, the gasoline tax revenues must be covered over because the gasoline tax is in all respects similar to the liquor and tobacco taxes, the revenues from which have traditionally been covered over. We conclude, however, that the United States correctly withheld the gasoline tax revenues, and that the District Court erred in ordering the United States to cover over these funds.

This case abounds in ambiguities, as the Government readily admits. It may be useful, therefore, to precede the detailed discussion that follows with a brief summary of the considerations we believe to be determinative.

In 1901 the Foraker Act dealt generously with Puerto Rico by exempting it generally from United States taxation. In the course of doing so, however, Congress recognized that mainland manufacturers subject to an excise tax on manufacture would be unfairly disadvantaged if Puerto Rican manufacturers making the same product were not subject to an equivalent tax. To equalize the competitive positions of the two, the Foraker Act provided that articles made in Puerto Rico and sent to the mainland market should be subject to an excise tax on manufacture at the same rate as that laid in respect of mainland manufacturers. Thus, for example, Puerto Rican manufacturers of cigars and spirits would have to pay an excise tax on those goods in the same way and in the same amount as a mainland cigar maker and distiller was required to pay.

For many years these excise taxes collected on Puerto Rican products were retained in the United States Treasury. When Congress passed the Jones Act in 1917, it decided, in order to ease the financial plight of Puerto Rico, to cover over these excise taxes collected in Puerto Rico into the Puerto Rican Treasury.

In 1956 the refining of gasoline first began in Puerto Rico. But there was not then, nor has there been since, any excise tax imposed by the United States on the manufacture of gasoline. In contrast with a distiller who becomes liable for a tax when whiskey comes into being, no tax is levied upon gasoline until it is first sold by the producer or the importer. Thus, Puerto Rican and mainland gasoline meet in the market on equal terms, and there is no occasion to equalize their competitive positions by taxing the manufacture of gasoline in Puerto Rico. There being no such tax, there is nothing to cover over into the Puerto Rican Treasury in respect of gasoline.

In so holding, we reach two conclusions: (1) that Congress intended to cover over only those taxes laid for equalization purposes, and (2) that the gasoline tax statute is not such a tax. We examine each such conclusion in turn.

III

We consider, first, the linkage *vel non* of the cover over provision and the Foraker Act taxation provision. The cover over statute at issue provides:

> All taxes collected under the internal revenue laws of the United States on articles produced in Puerto Rico and transported to the United States (less the estimated amount necessary for payment of refunds, and drawbacks), or consumed in the island, shall be covered into the treasury of Puerto Rico.

26 U.S.C. § 7652(a)(3) (1976). We begin by observing that the cover over provision is *not* clear and unambiguous, contrary to the District Court's assertion.[3] Rather, the cover over provision is replete with ambiguities requiring recourse to traditional methods of statutory construction.[4]

Primary among these ambiguities is the meaning of the phrase "all taxes" in the context of the cover over provision. Interpreted literally, the statute requires the covering over of all tax revenues ever collected when an article from Puerto Rico later becomes the subject of a taxable transaction in the United States: this would require the covering over even of estate and gift taxes levied years after the article entered the United States and mixed with domestic goods in the general market.

The administrative problems inherent in such a reading of the cover over provision are truly staggering. To effectuate this interpretation, Congress would have to separate Puerto Rican goods from other articles before sale, after sale, and throughout the useful life of the article, or else

[3] Commonwealth of Puerto Rico v. Blumenthal, No. 75-1035 (D.D.C. Oct. 10, 1978), slip op. at 8-11.

[4] These include the legislative history, administrative constructions, and policies underlying the statutory language. *Cf.* United Steelworkers of America v. Weber, 443 U.S. 193, 200-209 (1979).

develop tracing procedures for every type of article that Puerto Rico transports to the United States. Both scenarios are so impossible, both of conception and of practical application, as to render such a broad interpretation ridiculous. Indeed, even Puerto Rico admits that such an interpretation is "absurd." Brief for Appellee at 5-6 n.7. We must conclude that the phrase "all taxes" is, in the context of a cover over statute, ambiguous, requiring some form of modification or limitation.[5]

Given this initial ambiguity, the modifying phrase "on articles produced in Puerto Rico and transported to the United States" assumes crucial importance, yet it too is ambiguous. It is unclear from the language of the statute whether this phrase describes the taxable event—taxes laid primarily because the article is produced in Puerto Rico and transported to the United States—or instead is intended to describe a class of articles, all or some of the taxes upon which must be covered over into the island treasury. The scope of the cover over provision varies tremendously with the meaning of this phrase.[6] Yet, on its face, the phrase is susceptible to either interpretation.

[5] *See* Kananen v. Matthews, 555 F.2d 667 (8th Cir.), *cert. denied*, 434 U.S. 939 (1977) [courts have some scope for adopting a restricted rather than a literal reading of statute's words when the literal meaning would lead to absurd results]; Organized Migrants in Community Action v. Brennan, 520 F.2d 1161, 1166 (D.C. Cir. 1976) ["literal meaning will not be followed when it appears that to do so would, in view of the purpose of that statute, lead to an absurd or unjust result"]; International Tel. & Tel. Corp. v. General Tel. & Elec. Corp., 518 F.2d 913, 921 (9th Cir. 1975) [reference to legislative history is appropriate when the statutory language is ambiguous or where a literal interpretation would thwart the overall statutory scheme].

[6] If the phrase modifies "all taxes," limiting the taxes to those with the *taxable event* of production in Puerto Rico and transportation to the United States, then it follows logically that the cover over provision applies to Foraker Act taxes. A Foraker

Contrary to the District Court's holding, then, we find that the cover over provision is highly ambiguous. We therefore must resort to the traditional statutory interpretation aids, such as legislative history and administrative construction, in order to determine the scope of the cover over provision.

A. *Legislative History*

The legislative histories of the Foraker and Jones Acts show that the two provisions at issue were enacted at different times for apparently different purposes. Nevertheless, this by no means renders the two provisions unrelated or contradictory. On the contrary, the legislative histories of both provisions indicate that the two are interrelated; in fact, the cover over provision is most logically explained as an outgrowth of the Foraker "equalization tax" provision.

1. *The Foraker Act*

The Foraker Act, 31 Stat. 77 (1900), was Congress's first attempt to provide a government and economic struc-

Act tax is laid whenever an article transported from Puerto Rico into the United States to compete with other similar goods has escaped a tax laid on similar domestic goods and will operate in the mainland market at an unfair commercial advantage absent the levying of an equal tax. Several conditions must be met, one of which is necessarily an article's production in Puerto Rico (so that it escapes a tax purely by virtue of its origin) and its transportation to the United States (so that it stands to compete with taxed domestic goods). *See* text accompanying notes 9–11 *infra*.

If, however, the phrase modifies "all taxes" only insofar as it describes a class of articles, all of the taxes on which are to be covered over into Puerto Rico, nothing in the statute on its face suggests that the gasoline tax revenues should escape cover over.

ture for the newly acquired territory of Puerto Rico.[7] Most important of the Foraker Act provisions, for purposes of this case, was the imposition of a permanent tax in section 3. Section 3 provided, in relevant part, for the

> (imposition) upon articles of merchandise of Porto Rican manufacture coming into the United States and withdrawn from consumption or sale . . . [of] a tax equal to the internal revenue tax imposed in the United States upon the like articles of merchandise of domestic manufacture; . . . and on all articles of merchandise of United States manufacture coming into Porto Rico . . . [of] a tax equal to the internal revenue tax imposed in Porto Rico upon the like articles of Porto Rican manufacture.

Foraker Act, § 3, 31 Stat. 77 (1900) (current versions at 26 U.S.C. §§ 7652(a)(1) and 7653 (1976)). No special treatment of the revenues collected under this tax was required by the Foraker Act, and until 1917 all revenues collected pursuant to the provision were retained by the United States Treasury.[8]

This provision can accurately be termed an "equalization tax," because it was enacted to plug a loophole created by Congress's decision, in section 14 of the Foraker Act, to exempt Puerto Rico from the internal revenue laws of the United States.[9] As Representative Payne, Chairman of

[7] For a general discussion of its purposes, see H.R. Rep. No. 249, 56th Cong., 1st Sess. 1-6 (1900); 33 Cong. Rec. 1944, 2477 (1900).

[8] Another portion of section 3 required the United States to hold revenues from certain temporary customs duties for the benefit of Puerto Rico, but only until the President of the United States issued a proclamation creating a local government and system of taxation for Puerto Rico, at which time the duties ceased. *See also* H.R. Rep. No. 77, 64th Cong., 1st Sess. 1-2 (1916); H.R. Rep. No. 2945, 59th Cong., 1st Sess. 2 (1906).

[9] Section 14 of the Foraker Act provided that the internal revenue laws of the United States should not be applicable in

the Committee reporting the bill, explained on the floor of the House:

> [i]t occurred to me at once that if we allowed Puerto Rico cigars to come in here without paying an internal-revenue tax, it placed our people at a disadvantage. Our manufacturers would have to pay the 25 per cent of the duties . . . and in addition they would have to pay the internal revenue tax. I thought the Cigar Makers' Union had a just grievance against the proposition.

33 Cong. Rec. 1944 (1900). *See also* 33 Cong. Rec. 2477, 3515 (1900) (remarks of Sen. Foraker). Representative Payne alluded specifically to the manufacturer's excise tax on tobacco, which was imposed only on tobacco produced in the United States or imported into the United States from a foreign country. By excluding Puerto Rico from the internal revenue laws, Congress had held, in effect, that Puerto Rican tobacco was neither domestic nor foreign, and therefore would escape tax absent the Foraker Act tax.

This interpretation of the tax provision pervades the legislative history of the Foraker Act. As was stated in the Committee Report accompanying the bill, "The last provision [section 3] is necessary in order that our manufacturers of cigars and spirits may be at no disadvantage on account of the low tariff between Puerto Rico and the United States, on account of our internal revenue laws." H.R. Rep. No. 249, 56th Cong., 1st Sess. 1-2 (1900). This reading was also adopted by the Supreme Court in *Jordan v. Roche*, 228 U.S. 436, 443 (1913), in which the Court stated that "[t]he purpose of the Foraker Act was the

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Puerto Rico. As the Government noted in its brief on appeal, "The Congress believed that the excise taxes that then characterized the internal revenue system of the United States would unduly burden the people of Puerto Rico." Brief for Appellant at 23. *See* H.R. Rep. No. 249, 56th Cong., 1st Sess. 16 (1900).

equal taxation of Porto Rican articles and domestic articles."

It is most important that we define clearly the scope of the Foraker taxation provision now codified at 26 U.S.C. § 7652(a)(1) (1976), since the ultimate disposition of this suit turns on whether the tax laid on gasoline shipped from Puerto Rico to the United States since 1956 was levied pursuant to the Foraker tax provision or to 26 U.S.C. § 4081(a) (1976). Fortunately, the legislative history of the Foraker Act allows us to draw three unequivocal conclusions regarding the statute's purpose and scope.

First, the Foraker tax provision functions purely as an "equalization" provision. This is clear from both the purpose and the form of the statute. It was intended to equalize competition in those situations in which a Puerto Rican article being transported into the mainland market would have escaped a tax laid on similar domestic goods purely because of the peculiar tax status of Puerto Rico. Thus, the equalization tax comes into play not because of the manufacture, importation, or sale of the article—the usual taxable events found in tax statutes—but because of the existence of some domestic tax which, due to Puerto Rico's exemption from tax, reaches articles produced on the mainland but does not reach comparable goods in Puerto Rico. That the Foraker tax provision is triggered by the levying of some domestic tax threatening to skew competition is reflected in the form of the statute. It requires the imposition of a tax "equal" to one imposed in the United States on similar domestic goods.

A second precondition is apparent from the purpose of the statute and is reflected in the statutory language: the domestic tax must be laid at some point in the commercial cycle when the Puerto Rican article is exempt from United States tax. The Internal Revenue Service ("IRS") has interpreted this to mean that the domestic tax must be laid on the act of manufacture. *See* O'Connell letter, III-B *infra*. Congress's focus on the liquor and alcohol taxes

(both manufacturer's excise taxes) further strengthens the assumption that the domestic tax at issue will generally be a tax on manufacture, because such taxes clearly fail to reach articles of Puerto Rican manufacture.[10]

Third, the article must be manufactured in Puerto Rico and shipped to the United States for sale. The equalization tax was intended to apply only where an anticompetitive situation might be created due to a domestic tax, and this can only occur when the Puerto Rican article is brought into competition with the taxed domestic article.

On the basis of the statute's legislative history and language, then, we read the Foraker Act as imposing an equalization tax, as a condition of entry into the mainland market, on any Puerto Rican article that has escaped a tax previously laid on comparable American-made articles. Only when this equalization function is needed does the Foraker provision come into play. Furthermore, as far as we can discern, only domestic taxes on manufacture require such equalization. Any tax that applies equally to Puerto Rican and mainland goods, such as a tax on sale, does not require the application of a "mirror-like" equalization tax. It is primarily on the basis of this conclusion, that the Foraker provision imposes an equalization tax, that we eventually conclude that the gasoline tax revenues at issue need not be covered over.[11]

[10] We do not, however, foreclose the possibility that some tax other than a tax on manufacture exists requiring the application of a Foraker tax. We can think of no such example, but that does not mean that some future legislative enactment may not fit this description.

[11] The question arises whether this interpretation of the Foraker tax, as an "equalization tax," does not in fact nullify the charitable attempt to ease tax burdens on Puerto Rico through the blanket exemption in section 14. In fact, it does not. The Foraker tax does not come into play in a wide variety of situations; it applies only to taxes on articles shipped to the United States. Puerto Rican manufacturers who sell their wares locally

2. *The Jones Act*

The cover over provision, now codified at 26 U.S.C. § 7652(a)(3) (1976), was first enacted in 1917 as section 9 of the Jones Act, also termed the Second Organic Act, 39 Stat. 951, which dealt principally with the civil government and trade relations of Puerto Rico. H.R. Rep. No. 77, 64th Cong., 1st Sess. 1-2 (1916). As originally phrased, the statute provided:

> That hereafter all taxes collected under the internal-revenue laws of the United States on articles produced in Porto Rico and transported to the United States, or consumed in the island shall be covered into the Treasury of Porto Rico.

Jones Act, § 9, 39 Stat. 951 (1917).

The purpose of the cover over provision becomes clear within its historical context. Puerto Rico, a small, resource-poor island, was then, as now, dependent on imports for its necessities. In the years preceding the First World War, Puerto Rico imported European goods upon which it could impose customs duties. With the outbreak of the war, however, trade with Europe was disrupted and Puerto Rico was forced to rely on duty-free imports from the United States, losing a tremendous amount of revenue as a result. H.R. Rep. No. 77, 64th Cong., 1st Sess. 1-2 (1916). To remedy this situation, Congress enacted the cover over provision. As the House Committee on Insular Affairs noted, "The loss of this revenue has seriously embarrassed the Porto Rican Government, and it is believed to be but just and fair that it should receive the internal revenue taxes collected upon its products." *Id.*

3. *Linkage of the Two Provisions*

As to the general purposes of the two provisions, the parties herein do not disagree. The scope of the cover over

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are exempt from taxation by the United States (though still liable for taxation by Puerto Rico). Also, the Foraker Act did not lift the exemption from taxes on occupations, only from taxes on *articles transported*.

provision, however, is hotly disputed and represents the major question for our determination.

The District Court argued that Congress, recognizing Puerto Rico's precarious economic situation, intended the cover over provision to be broad. The court cited language in the legislative history of the Jones Act wherein the Senate Committee on Pacific Islands and Porto Rico ascribed a broad charitable purpose to the cover over provision and noted that the provision should be "all inclusive." S. Rep. No. 579, 64th Cong., 1st Sess. 2 (1916). From this, the court concluded that Congress intended to cover over more than just equalization taxes. *Commonwealth of Puerto Rico v. Blumenthal*, No. 75–1035, at 9–11.

The United States argues from the same language that Congress intended the cover over provision to apply to all equalization taxes, but to no other taxes. We find the United States's argument the more convincing in four respects.

First, the original drafted form of the cover over provision indicates Congress's assumption that only equalization tax revenues would be affected by the cover over provision. Although the cover over provision currently stands alone as 26 U.S.C. § 7652(a)(3) (1976), in its original drafting it was phrased as a *proviso* to another portion of the Jones Act:

> That the statutory laws of the United States not locally inapplicable, except as hereinbefore or hereinafter otherwise provided, shall have the same force and effect in Porto Rico as in the United States, *except the internal-revenue laws: Provided, however*, that hereafter all taxes collected under the internal-revenue laws of the United States on articles produced in Porto Rico and transported to the United States, or consumed in the island shall be covered into the treasury of Porto Rico.

39 Stat. 951 (emphasis added).

On its face, this is an odd construction, since the cover

over provision is apparently an extension of the favorable treatment of Puerto Rico implicit in its exemption from the internal revenue laws (App. 88). This construction makes sense only if an assumption is read in: that the cover over proviso refers to the equalization taxes, which truly do limit the benefits Puerto Rico derives from the exemption. Once this is assumed, the linkage of the exemption and the cover over provision becomes quite logical: Congress decided to limit the blanket exemption by imposing equalization taxes and by rebating those revenues to the Puerto Rican government, not to the people directly.

This interpretation is strengthened by the restatement, in the Jones Act, of the blanket exemption first passed as Section 14 of the Foraker Act. The Foraker Act originally provided that "the internal revenue laws . . . *in view of the provisions of section three* [the Foraker tax provision], shall not have force and effect in Puerto Rico." Foraker Act, § 14, 31 Stat. 77, 80 (1900) (emphasis added). That Congress restated this provision in the Jones Act suggests that the new exemption was also enacted "in view of" the Foraker tax.

Equally as telling is the legislative history accompanying the Jones Act. In explaining the addition of a cover over provision to the previously enacted exemption, the House Committee on Insular Affairs stated:

> It appears that the present rule is to pay into the Porto Rican treasury those taxes that are collected under the internal-revenue laws of the United States on articles produced and used in Porto Rico, and into the Treasury of the United States internal-revenue taxes collected on articles produced in Porto Rico but transported to the United States.

H.R. Rep. No. 77, 64th Cong., 1st Sess. 1-2 (1916). This describes, albeit rather inaccurately, the treatment of

taxes collected pursuant to the equalization tax provision.[12] The Committee report then continued:

> In the opinion of your committee *these taxes* should all be covered into the treasury of Porto Rico . . . The customs duties collected in Porto Rico have fallen off in the last three or four years . . . The loss of this revenue has seriously embarrassed the Porto Rican Government, and it is believed to be but just and fair that it should receive the internal-revenue taxes collected upon its products, whether those products are used in Porto Rico or produced in Porto Rico and transported and used in the United States.

Id. (emphasis added). The Committee clearly referred to the Foraker equalization taxes in calling for the covering over of "these taxes."

During the House debates, Representative Miller spoke in support of the cover over provision, using as an example tobacco taxes, which were specifically focused upon by the framers of the equalization tax. *See* 33 Cong. Rec. 1944 (1900). He described the taxes at issue as "excise taxes," on articles "consumed in the United States, having been imported from Puerto Rico," and then noted that "It is proposed in this bill *that that sum of money* shall go into the treasury of Puerto Rico." 53 Cong. Rec. 7475 (1916) (emphasis added). These are only two of numerous examples within the legislative history of framers' specific references to equalization taxes when discussing the scope of the new cover over provision. It is apparent that the cover over provision framers were not working in a vacuum; rather, they specifically considered a certain class of taxes

[12] The first portion of the description, "taxes that are collected under the internal-revenue laws of the United States on articles produced and used in Puerto Rico," refers to nonexistent taxes, since after section 14 of the Foraker Act was enacted, the United States did not tax Puerto Rican goods consumed in Puerto Rico. The second description, however, is an accurate description both of the Foraker equalization taxes and of their treatment.

when determining whether to enact the cover over provision. Never within the legislative history do we find a general description, such as "all inclusive," that is not preceded by a description of an equalization tax.

Throughout the legislative history accompanying the Jones Act, we also find less direct, but equally valuable, evidence that the taxes to be covered over were to be equalization taxes. In the House Report accompanying the Jones Act, the Committee used the amount that had been paid into the Treasury pursuant to the Foraker Act ($500,000) as a reasonable estimate of how much money Puerto Rico could expect to have covered over to its treasury in the future. H.R. Rep. No. 77, 64th Cong., 1st Sess. 2 (1917). And we note that the appellation "just" used by the House Committee in describing the cover over provision, *id.*, was almost a direct quotation from the House Report acompanying the Foraker Act and was used to describe the equalization tax provision. H.R. Rep. No. 249, 56th Cong., 1st Sess. 6 (1900).

The fourth and most decisive factor indicating the linkage of the two provisions was the amendment of the cover over provision on the floor of the Senate. When the cover over provision came to the Senate floor for a vote, it extended only to articles "manufactured in Puerto Rico and transported to the United States." The Senate amended it to apply to goods "manufactured in Porto Rico and transported to the United States, or consumed in the island."

Puerto Rico and the District Court have made much of this amendment, arguing that it devastates the United States' argument by extending the cover over provision to taxes that are not equalization taxes.[13] On the contrary, this amendment is powerful evidence in the United States's favor. As we noted above, the equalization tax applied *quid pro quo*, providing for the imposition not only of a tax

[13] *See* Commonwealth of Puerto Rico v. Blumenthal, No. 75-1035 at 11; Brief for Appellee at 11 n.13.

on goods manufactured in Puerto Rico and transported to the United States, but also of a complementary tax "on all articles of merchandise of United States manufacture coming into Porto Rico . . . of a tax equal in rate and amount to the internal-revenue tax imposed in Porto Rico upon the like articles of Porto Rican manufacture."[14]

By amending the cover over provision to include articles "consumed in the island," Congress made the cover over provision perfectly coextensive with the Foraker equalization tax. The conclusion is inescapable that Congress did so intentionally. The phrase "consumed in the island" could only have applied to taxes laid pursuant to the equalization tax, since Congress had provided that all other internal revenue taxes would not apply "in Puerto Rico." Foraker Act, § 14, 31 Stat. 77 (1900). Puerto Rico's argument—that this clause applies to other United States taxes laid on locally manufactured and consumed goods—is simply incorrect, since no such taxes existed.

Thus, the phrase "consumed in the island" is meaningless unless it applies to the equalization tax laid on goods transported from the United States to Puerto Rico. Furthermore, for Congress to have amended the statute to cover exactly *all* of the equalization taxes indicates an intent to limit the cover over provision accordingly. We conclude that the amendment was intended to tie the cover over provision more closely to the Foraker equalization tax provision and to make the two provisions identical in scope.

Puerto Rico challenges our reading of the legislative history on three grounds. First, Puerto Rico points to the broad descriptions of the cover over provision that are contained within the legislative history, the most obvious being the description of the Senate amendment as having made the cover over provision "all inclusive, which is the

[14] *See* Section III-A-1 *supra*, for the complete text of the original Foraker equalization tax provision.

intent." S. Rep. No. 579, 64th Cong., 1st Sess. 2 (1916). As we have noted above, though, the Senate amendment merely extended the cover over provision to the only remaining portion of Foraker equalization taxes not yet included in the cover over provision; thus, the amendment certainly is not authority for the proposition that the cover over provision is broader than the equalization tax provision. Rather, given the nature of the amendment, the "all inclusive" language likely refers to inclusion of *all* equalization taxes.

More generally, Puerto Rico challenges any conclusion, on the basis of the legislative history, that the cover over provision is limited to equalization taxes. Although Congress may have been considering equalization taxes in framing the statute, Puerto Rico argues, Congress in no way evinced an intent to so limit the cover over provision's scope. This is especially true since, at the time the cover over provision was passed, the only taxes on Puerto Rican liquor and tobacco, Congress's greatest concerns, were equalization taxes; the retail sales tax and War Excise taxes had not yet been enacted.[15] We are urged not to interpret Congress's allusions to equalization taxes, then, as signs that Congress intended to limit the seemingly expansive language of the cover over statute.

This argument is true as far as it goes, in that legislative intent to include certain specific taxes does not necessarily exclude other taxes of a similar genre that may be enacted at some future time. *Jordan v. Roche*, 228 U.S. 436, 443 (1913) ["the internal revenue laws do not describe articles by name but by character"]. In this instance, however, we believe this fact cuts the other way, to explain why Congress did not limit the cover over provision to Foraker taxes in a more specific manner.

In this particular case we are convinced that Congress specifically intended to cover over only equalization taxes.

[15] *See* Brief for Appellant at 28; Commonwealth of Puerto Rico v. Blumenthal, No. 75-1035, at 10-11.

Congress amended the cover over provision to be exactly coextensive with the Foraker Act, which indicates a specific focus on the equalization taxes. Furthermore, those legislators who described the purview of the cover over provision uniformly described the covered taxes by *genre:* taxes on "those articles manufactured in Puerto Rico and transported to the United States."[16] The District Court cited these general descriptions for the proposition that the cover over tax is broader than the equalization tax, but we think the better interpretation is that Congress intended the cover over provision to cover *all* equalization taxes and *no* others. Third, the original drafted form of the cover over provision suggests that Congress assumed the cover over provision applied only to equalization taxes. Once it is assumed that the peculiar "proviso" form of the original drafting indicates this linkage, it follows inescapably that the proviso applies only to equalization taxes since the "proviso" construction would be illogical applied to any but equalization taxes. Thus, the cover over and equalization taxes seem closely linked, and Congress's intent to link them, regardless of later tax developments, is a sound conclusion.

Finally, we address Puerto Rico's general policy contention, which was adopted by the District Court in its opinion, that these two provisions cannot be linked because they were enacted at different times for different purposes. The argument, as phrased by Puerto Rico, is that the two provisions "derived from two entirely different statutes, enacted for totally different purposes seventeen years apart." Brief for Appellee at 11. The implicit assumption is that the latter statute—the cover over provision—contradicted the former at least in spirit.

Since we have just interpreted the legislative history of the Jones Act to indicate that the cover over provision applies only to equalization taxes, this argument would seem to be moot. If Congress in fact considered the two

[16] *See* 53 Cong. Rec. 7475 (1916) (remarks of Rep. Miller).

provisions related and acted upon that assumption, as we have held to be the case, neither Puerto Rico nor any court may interpose a different interpretation as a matter of hindsight.

But even if the legislative history were inconclusive, we could not accept the premise that the two statutes are contradictory in spirit and therefore irreconcilable. On the contrary, we believe that these enunciated "contradictory" goals, while accurate descriptions of the purposes behind the two provisions, are oversimplifications of Congress's purposes for passing the two Acts *in toto*. Considered in tandem, the two Acts appear intimately related, such that the latter statute—the cover over provision—is a logical outgrowth of the former.

The equalization taxation provision was in fact inspired by protectionist sentiments, while the cover over provision was primarily designed to bring revenue into the coffers of the Government of Puerto Rico. But it is quite inaccurate to label the equalization tax "protectionist" and the cover over provision "charitable" and abandon all attempts to reconcile the two. The equalization tax was made necessary only because Congress, elsewhere in the Foraker Act, indulged its charitable impulses toward Puerto Rico by exempting Puerto Rico from tax.[17] Thus, it is gross oversimplification to label the equalization tax merely a "protectionist" gesture. Rather, the tax represents an informed decision by Congress to balance its charitable impulses toward Puerto Rico against the need to protect mainland manufacturers from the results of Congress's altruism.

Similarly, the Jones Act cover over provision cannot be viewed in a vacuum. The thrust of the Jones Act was not simply charity toward Puerto Rico; the Act was intended primarily to integrate Puerto Rico into the United States federation to give its citizens the benefits of United States

[17] Foraker Act, § 14, 31 Stat. 77 (1900).

citizenship.[18] The Jones Act as a whole thus evidences a balancing process similar to that which occurred in the Foraker Act. Together the Foraker and Jones Acts can be seen as an ongoing attempt to enact a body of laws benefiting Puerto Rico and not injuring the United States mainland, and all the provisions of both Acts can be seen as means toward that end. The Jones Act debates contain numerous allusions to the Foraker Act,[19] and the tone of the debates indicates that Congress envisioned itself as improving upon reforms begun in the Foraker Act.[20] Notably, the two Acts were generally referred to as the "First and Second Organic Acts." Any assumption that their pro-

[18] A large portion of the Jones Act debates was consumed with discussion of whether Puerto Ricans should be given United States citizenship, a proposition which, given the terms of the bargain, many Puerto Ricans did not support. 53 Cong. Rec. 7470–7480 (1916). In the debates, Congress seemed primarily concerned with the long-term political stability of the island. *Id.* The cover over provision received little attention. *See* 53 Cong. Rec. 7475 (1916) (Rep. Miller's brief discussion of the cover over provision).

[19] Most notably, Representative Miller described the taxes collected pursuant to the Foraker Act, and their treatment prior to 1916, and then stated, "[T]hat is one of the changes made in the bill." 53 Cong. Rec. 7475 (1916). He then went on to describe the tobacco taxes upon which the framers of the Foraker tax concentrated, *see* 33 Cong. Rec. 1944 (1900) (remarks of Rep. Payne). Representative Miller concluded by remarking, "It is proposed in this bill that *that sum of money* shall go into the treasury of Porto Rico" (emphasis added).

[20] The Jones Act was intended primarily to supersede those portions of the Foraker Act creating a provisional government. 53 Cong. Rec. 7470–7473 (1916). Apart from criticizing the government created by the Foraker Act, the Congressmen and Puerto Rican witnesses discussing the Jones Act had high praise for the Foraker Act reforms (such as the public school system). *See* 53 Cong. Rec. 7470–7475 (1916) (particularly the remarks of Mr. Rivera).

visions are mutually exclusive is, therefore, unsupported by the Acts themselves.

But even if the Jones Act had represented a departure from earlier legislative policy, it is simply illogical to assume that the Congress enacting the Jones Act would not have made use of the equalization tax provision if that had seemed a logical and fair manner of aiding Puerto Rico. In enacting statutes to meet current needs, Congress does not ignore all statutes that went before, merely because those older statutes were enacted to meet different needs. In such a situation, the test is not the purposes of the statutes, but the statutory language—whether the two statutes can coexist and, together, effectuate some desired legislative policy. Nothing in these two statutes prevents their coexistence, and, more important, nothing prevents their linkage.

In fact, to assume that two such statutes could not coexist seems especially fallacious in this instance. The Foraker tax provision generates a discrete body of taxes, all collected at the same time, the covering over of which would be administratively simple, extremely helpful to Puerto Rico, and, in a sense, rather "just and fair" since the equalization taxes were imposed not for general revenue purposes benefiting all Americans, but for the purpose of protecting mainland manufacturers. To assume that Congress, in enacting a "charitable" provision, would not have made use of such an obvious tool simply because the tool was originally enacted for another purpose is simply unrealistic.

Of course, the fact that we can, with hindsight, see the covering over of Foraker taxes as a logical solution to Puerto Rico's dilemma does not mean that this was the route chosen by Congress; we cannot read our legislative preferences into the law. But it does cast doubt on Puerto Rico's assertion that Congress *could not* have intended to cover over only equalization taxes.

In sum, we read the legislative history surrounding the

passage of the cover over provision and the subsequent amendment of the statute to indicate that Congress intended to limit the scope of the cover over provision to Foraker taxes. While there are phrases within the legislative history susceptible to multiple interpretations, only the United States's interpretation of the cover over provision is consistent with (1) the overall purposes of both Organic Acts, (2) the original drafting of the statute, (3) the numerous references within the legislative history indicating that the cover over provision was tied to previous legislative enactments, and (4) the amendment of the statute to be absolutely coextensive with the equalization tax.

We also base our interpretation of the cover over provision, to a very great extent, on the inability of the District Court to marshal any legislative history supporting its exceedingly broad interpretation, or else to limit that broad interpretation in a principled fashion. The District Court and Puerto Rico completely ignore the fact that the broad language of the statute must be limited in some fashion, or else the "plain meaning" of the statute requires an absurd result. Our interpretation is, in our view, more consistent with Congress's ongoing attempt to benefit Puerto Rico without unduly harming mainland Americans.

B. *Administrative Constructions*

The District Court pretermitted any discussion of administrative constructions of the cover over provision by interpreting the cover over provision according to its "plain meaning." But, having held that the statute is by no means unambiguous, we undertake an examination of the administrative constructions of the cover over provision by the United States Treasury, the government agency charged with the statute's enforcement. The interpretation of a statute by that federal agency charged with the statute's enforcement is entitled to great weight in a court's construction of ambiguous statutory language,[21]

[21] Zenith Radio Corp. v. United States, 437 U.S. 443 (1978). *Accord*, Saxbe v. Bustos, 419 U.S. 65, 75 (1974); Udall v.

especially when, as in this case, "Congress has opted for legislative generality, leaving the agency with the task of definition on a case-by-case basis." *Chisholm v. Federal Communications Commission*, 538 F.2d 349, 358 (D.C. Cir.), *cert. denied*, 429 U.S. 90 (1976).

We find that a consistent administrative interpretation of the cover over provision supports our reading of the legislative history. The Treasury has repeatedly held that the cover over provision applies only to equalization taxes. These interpretations are entitled to great weight because they are both consistent and public. The Treasury has adhered to the same basic interpretation of the cover over provision for 50 years, and Puerto Rico has never challenged this interpretation nor Congress amended the statute to override this interpretation.

We rely on four major administrative constructions. The best publicized administrative interpretation of the cover over provision was undertaken by Acting Secretary of the Treasury O'Connell, in a letter transmitted to the Senate Finance Committee in 1947,[22] when the Senate was considering enacting an analogous cover over provision (S. 1014) for the Virgin Islands.[23] In his letter, the Acting

Tallman, 380 U.S. 1, 16 (1965). *See also* Gelman v. Federal Election Commission, (D.C. Cir. July 18, 1980), slip op. at 9; Kyle v. Interstate Commerce Commission, 609 F.2d 549 (D.C. Cir. 1979).

[22]The O'Connell letter was incorporated into the Committee Report, S. Rep. No. 476, 80th Cong., 1st Sess. 5-6 (1947), and placed on record during hearings before the House Ways and Means Committee in 1948 on a bill similar to S. 1014. *See* Hearings on H.B. 4979 before the House Committee on Ways and Means, 80th Cong., 2d Sess. 54 (1947).

[23]S. 1014 was not enacted by Congress, but seven years later Congress enacted a cover over provision that we are assuming to be identical in effect to that applying in Puerto Rico. *See* section II *supra*. Puerto Rico's argument that we should not consider the legislative history of a bill that was never enacted rep-

Secretary interpreted the Puerto Rico cover over provision as follows:

> It is the understanding of the Department that, insofar as S. 1014 relates to the internal revenue taxes collected upon articles produced in the Virgin Islands and transported to the United States, the tax proceeds segregated by the bill to the Virgin Islands are *. . . such taxes as are due and payable at the time the Virgin Islands article is withdrawn from customs for the consumption or sale in the United States.* It is the further understanding of the Department *that the bill does not cover taxes collected with respect to Virgin Islands articles after they have entered within the United States; that is that the bill does not cover such taxes as Federal retail sales taxes collected with respect to Virgin Islands articles sold at retail in the United States*, nor the tax on manufactured sugar which may be paid by the manufacturer under section 3490 of the Internal Revenue Code with respect to Virgin Islands raw sugar refined in the United States *. . . The views expressed above as to the internal revenue taxes covered by S. 1014 are the construction which the Department has given to section 3360(a) [now the Puerto Rico cover over provision codified at 26 U.S.C. § 7652(a)(3) (1976)] of the Code in the case of internal revenue taxes segregated to Puerto Rico.*

(App. 25) (emphasis added).

In so holding, O'Connell held that the cover over provision applies only to those taxes we have identified as equalization taxes: those taxes imposed as conditions of entry into the United States, not those domestic taxes im-

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resents a correct statement of the law, Interstate Natural Gas Co. v. F.P.C., 156 F.2d 949, 952 (5th Cir. 1946), *aff'd.*, 331 U.S. 682 (1947), but it is a principle inapplicable to the case at hand. We are examining the O'Connell letter not as legislative history of S. 1014, but as a Treasury construction of the Puerto Rico cover over provision.

posed on all goods alike after the goods enter the mainland market.[24]

The Treasury again undertook an exhaustive discussion of the cover over provision in a memorandum from Chief Counsel Oliphant of the IRS to Deputy Commissioner Valaer, dated July 9, 1951. (Doc. C-62) (App. 366). In this memorandum Oliphant determined that the cover over provision applies only to Foraker equalization taxes. His conclusion was based, first, on the equalization purpose of the Foraker tax provision. Given this, he said, clearly the Foraker provision was not intended to extend to any taxes "the liability for which would not attach until after the Puerto Rican goods have entered into commerce within the United States." (App. 369). No equalization is necessary in such a case.

Oliphant went on to conclude that only equalization taxes need be covered over to Puerto Rico. He noted that the same factor making equalization unnecessary—taxation after the Puerto Rican and mainland goods enter the United States market on equal terms—also makes cover over of such tax revenues impossible, absent tracing (App. 370). Furthermore, he noted briefly that cover over of any taxes from which Puerto Rico was never exempt in the first place seems fundamentally illogical. *Id.* Oliphant's ultimate conclusion—that only liquor and tobacco require equalization taxes—has since been repudiated by the IRS, in favor of a more general view comporting with our interpretation herein,[25] but this in no

[24] *See* Section III-A-1 *supra*.

[25] In Revenue Ruling 58-554, 1958-2 C.B. 909, the IRS held that application of the equalization tax provision depends not on the nature of the article but on the nature of the *domestic tax* laid on that article. This comports with our interpretation of the Foraker equalization tax discussed at III-A-1 *supra*. Since the IRS released Revenue Ruling 58-554, the Treasury has examined the applicability of the Foraker tax to Puerto Rican margarine (Doc. C-57) (App. 316) and Puerto Rican ballpoint pens

way undercuts the validity of his general argument, which is closely tied both to the legislative purpose of the two provisions and to simple logic.

A shorter IRS file memorandum reiterated this interpretation of the cover over provision to apply only to those revenues from taxes imposed upon manufacture or before withdrawal for sale. Doc. C-6, May 1, 1947 (App. 360-365). The author of this file memorandum clearly linked the cover over and the equalization tax provisions. He noted that the purpose of the Foraker tax is to equalize competition, and this is necessary only when the article escapes a tax laid before that article reaches the mainland. As he stated,

> After articles have entered the country, been merged with the commerce of the United States, if they have become subject to Federal retail or manufactures tax, or processing tax, tax proceeds have never been segregated to the Philippines or Puerto Rico unless specifically directed by statute.

Doc. C-7, May 1, 1947 (App. 365). He then held that taxes not imposed under the Foraker tax provision need not be covered over to the Treasury of Puerto Rico (App. 362).

The most detailed interpretation of the Foraker equalization tax provision appears in Revenue Ruling 58-554, 1958-2 C.B. 909, in which, as noted above,[26] the IRS overruled the narrow application of the equalization tax only to liquor and tobacco. In this ruling, the IRS also held that the equalization tax is triggered only by a domestic tax on the manufacture of goods, not by a tax on the sale of goods. This revenue ruling is of crucial importance because the IRS had occasion to consider directly the application of the equalization tax provision to the gasoline tax at issue here.

(Doc. H-15) (App. 372). *See* our discussion of Revenue Ruling 58-554 at text accompanying note 26 *infra*, for an examination of other aspects of this ruling.

[26] *See* note 25 and accompanying text *supra*.

This revenue ruling concluded that certain taxes imposed by Chapter 32 of the Code (including the gasoline tax) need not be covered over because

> the general wording of the statute, references thereto by Congress, and its purpose as expressed by the Supreme Court of the United States indicate that any articles may be so subjected, *provided the tax relating thereto is laid on the act of manufacturing rather than the act of sale.*

(emphasis added). The IRS explained:

> Administrative considerations and departmental policy further indicate that the only taxes imposed by section 7652 of the Code are those which can be imposed *at the time of entry of the goods into the United States or at the time they are withdrawn from places of government supervision. . . . a tax on the act of manufacturing, as distinguished from a tax on the act of sale, would be within the purview of section 7652 of the Code.* The manufacturers excise tax imposed by Chapter 32 of the Code and the retailers excise tax imposed by Chapter 31 of the Code are examples of taxes *excluded from* the meaning of the phrase "the internal revenue tax" in section 7652(a)(1) of the Code. *Those taxes are imposed on the sale and not on the act of manufacturing.*

(emphasis added).

The gravamen of the IRS ruling is on all fours with our view: the IRS reasoned that, since Chapter 32 taxes (including the gasoline tax) are imposed at the point of sale, they do not create the unequal tax burden requiring application of the equalization tax.

In sum, the Treasury has consistently interpreted the cover over and equalization tax provisions in a manner that comports with our view of the legislative history. The Treasury has held that only taxes payable at manufacture, as a condition of entry into the competitive market, trigger equalization taxes, and that only equalization taxes need be covered over. More important, the Treasury

reached this conclusion in a consideration of the specific gasoline tax at issue in this case. Rev. Ruling 58-554, 1958-2 C.B. 909.

Considering that these constructions are longstanding, consistent, and legally sound, we are not disposed to override them. We conclude that the cover over provision applies exclusively to those taxes laid pursuant to the equalization tax provision, 26 U.S.C. § 7652(a)(1) (1976).

IV

Our only remaining inquiry is whether the gasoline tax revenues sought by Puerto Rico and the Virgin Islands were collected pursuant to an equalization tax. If so, Congress has directed that these funds should be covered over to the island treasuries. We find ourselves in agreement with the IRS regarding this gasoline tax, however, and hold that it does not require application of the equalization tax. Gasoline is taxed at the point of sale, not manufacture; thus, Puerto Rican and mainland manufacturers meet in the market as equals. An examination of the gasoline statute, as compared to the liquor and tobacco statutes, clearly reveals this difference and compels this result.

The gasoline tax statute provides:

> There is hereby imposed on gasoline sold by the producer or importer thereof, or by any producer of gasoline, a tax of 4 cents a gallon.

26 U.S.C. § 4081(a) (1976). The alcohol and tobacco tax statutes, which the United States has long held to require application of the equalization tax, provide in relevant part:

> There is hereby imposed on all distilled spirits produced in or imported into the United States a tax at the rate of $10.50 on each proof gallon and a proportionate tax at the like rate on all fractional parts of a proof gallon . . .

> (c) *Cross reference.—For provisions relating to the tax on shipments to the United States of taxable articles from Puerto Rico and the Virgin Islands, see section 7652.*
>
> * * *
>
> On cigars, manufactured in or imported into the United States, there shall be imposed the following taxes . . . .

26 U.S.C. § 5001 (1976) (liquor tax); 26 U.S.C. § 5701 (1976) (tobacco tax). The crucial difference is immediately apparent: the gasoline tax is imposed upon gasoline "sold by the producer or importer thereof," while both the liquor and tobacco taxes are imposed upon the "manufacture" or "production" of the product.

We read the legislative history of the Foraker Act to require the imposition of an equalization tax only when a domestically laid tax has failed to reach a Puerto Rican article at the time the article enters into competition with domestic goods in the mainland market.[27] Here the Puerto Rican gasoline comes into direct competition with domestically manufactured gasoline, but, at the time they come into contact, no gasoline has yet been taxed and the Puerto Rican manufacturer has no competitive edge. The manufacturers meet as equals. Thus, one of the conditions we have postulated herein has not been fulfilled: domestic gasoline has not been subjected to a tax from which Puerto Rican gasoline remains exempt. The "protectionist" purpose of the equalization tax is not implicated.

This situation is in contrast to that which occurs when a tax is laid on the manufacture of cigars. The tax applies by its terms to cigars "manufactured in the United States" but, since Puerto Rico is not considered part of the United States for purposes of the internal revenue tax, the Puerto Rican manufacturer escapes the manufacturer's excise

[27] *See* Section III-A-1 *supra*.

tax. Under these circumstances, the equalization tax provision requires that a tax equal to the domestic tax on manufacture be collected before the good enters the competitive market and undersells the domestically manufactured product. This is exactly the process by which alcohol and tobacco shipped from Puerto Rico are taxed, either in Puerto Rico or upon entry into the United States and removal from bond. *See* 27 C.F.R. § 250.1–250.119 (1979).

Other characteristics of the gasoline tax make this difference even more pronounced. Section 4081, read in conjunction with its definitional statutes (sections 4082 and 4083), clearly indicates that the gasoline tax is a tax on *sale* applied to goods while they are in the United States, not in tax-exempt Puerto Rico. In 26 U.S.C. § 4082, Congress defines "producer" to include any "refiner, compounder, blender, or wholesale distributor, and a dealer selling gasoline exclusively to producers of gasoline, as well as a producer." Congress goes on to provide that "any person to whom gasoline is sold tax-free under this subpart shall be considered the producer of such gasoline." *Id.* In section 4083, Congress provided that the "tax imposed by section 4081 shall not apply in the case of sales of gasoline to a producer of gasoline." 26 U.S.C. § 4083 (1976).

In other words, gasoline can change hands within the United States indefinitely, without the taxable event occurring; the tax is not levied until some producer sells to a retailer. The taxable event could be long delayed, or it could occur on the first sale after the gasoline enters the country; the point is that Congress has clearly pinpointed *sale* as the taxable event.

As we noted above,[28] the IRS has considered this precise question and ratified our interpretation of the gasoline tax. In an explicit consideration of the gasoline tax, as well

[28] *See* text accompanying note 26 *supra*.

as of the other taxes in Chapter 32 of the 1954 Code, the IRS held that the Chapter 32 taxes are levied on sale, not manufacture, and therefore need not be covered over to Puerto Rico. Rev. Ruling 58-554, 1958-2 C.B. 909. But even if Revenue Ruling 58-554 did not specifically address this question, it adopts a view of the equalization tax—as being dependent on the domestic tax at issue—that would lead us inexorably to the same conclusion. The gasoline tax simply does not require the laying of an equalization tax. Therefore, the revenues it generates certainly are not equalization tax revenues suitable for cover over.

Puerto Rico argued, and the District Court held, that the difference in language between the gasoline tax statute and the liquor and tobacco taxes (domestic taxes long held to require application of the equalization tax) is irrelevant because the taxes are all functionally identical, but we find these arguments uniformly unpersuasive. First, the argument that the statutes are identical in language, or that their "minor" semantic differences should not be deemed significant because the taxes are otherwise identical,[29] is plainly without merit. The crucial inquiry is whether the gasoline tax is laid on the act of sale or manufacture, and the gasoline tax statute states plainly that a four cent tax will be laid on gasoline "sold," while the liquor and tobacco taxes are laid on articles "manufactured." This difference may be irrelevant in other contexts, but it is certainly determinative in this instance.[30]

Any attempt to portray the gasoline statute and the tobacco and liquor statutes as functionally identical is also doomed to fail. Regardless of where the incidence of the

[29] Brief for Appellee at 20.

[30] At any rate, the Supreme Court has mooted this argument, for purposes of the gasoline tax, by holding that the gasoline tax is levied at the point of sale to a retailer. Gurley v. Rhoden, 421 U.S. 200 (1975).

tax falls,[31] how the tax is measured,[32] or whether the gasoline tax resembles manufacturer's excise taxes in certain other trivial respects,[33] it is indisputably true that the

[31] In Gurley v. Rhoden, 421 U.S. 200 (1975), the Supreme Court held that the incidence of the gasoline tax falls on the producer who makes the taxable sale to the retailer, and not on the consumer. In fact, the Treasury has promulgated regulations to this effect. 26 C.F.R. § 48.480 4081-1(c) (1979). These regulations contain within them even more evidence that the gasoline tax is levied at the point of sale: "The tax imposed by section 4081 is payable by the producer or importer making the sale of the gasoline." *Id.* (emphasis added).

We feel that the question of who pays the tax is legally irrelevant. Regardless of who pays this tax (and, we emphasize, the tax may be paid by the manufacturer or any in a long line of middlemen), the tax liability arises at the point of *sale*. The Puerto Rican and mainland products meet in the market on equal terms, and no equalization is necessary.

[32] Puerto Rico argues that the gasoline tax is really a manufacturer's excise tax because it is computed without reference to market prices at the time the gasoline is sold; rather, a flat four cents a gallon tax is laid on each gallon sold or used. Brief for Appellee at 23. This merely proves that the gasoline tax is not a retail sales tax, which has never been argued herein. It is irrelevant to the crucial question: whether gasoline coming into the United States from Puerto Rico has already escaped a domestically laid tax on manufacture.

[33] Two other alleged similarities deserve mention. Puerto Rico argues that the gasoline tax is not a tax on sale because is is "imposed on the entirety of gasoline produced whether sold or not." Brief for Appellee at 22. Puerto Rico alludes to the fact that the IRS, by regulation, imposes the tax upon the sale or use of the gasoline. 26 C.F.R. § 48.4082-1(c) (1979).

This regulation, however, in no way undercuts our argument. In this regulation the IRS specifically analogizes certain types of uses to sales, and then proceeds to tax those uses as if they were sales. This only underscores our reading of the gasoline statute as a tax triggered by sale, not by manufacture.

The final argument worth considering is Puerto Rico's conten-

gasoline tax is laid on sale, while manufacturer's excise taxes such as liquor and tobacco taxes are laid on manufacture. Because the gasoline tax is laid on sale, it does not give Puerto Rican manufacturers any advantage when they bring their gasoline into the mainland market. The competitive statures of the manufacturers are equal, and no equalization tax is required.

By adopting Puerto Rico's arguments to the contrary, the District Court failed to recognize that *time of taxation* is the crucial inquiry, and that the gasoline statute differs from the others in this respect. As a result, the District Court erred in concluding that the gasoline tax revenues, past and future, must be covered over to the island treasuries. We reverse, and hold that the United States correctly withheld these tax revenues.

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tion that the tax liabilities for these three statutes actually occur at the same time. This is simply untrue. Liquor and tobacco are taxed in Puerto Rico before their shipment to the United States, or taxed upon release from warehouse or bond. 27 C.F.R. § 250.1-250.119 (1979). The regulations controlling this process are extremely complex. They include provisions for deferred payment of tax, and it is probably this provision upon which Puerto Rico bases its claim. But the difference is illusory. Regardless of when the manufacturer of liquor and tobacco actually pays the tax, the tax liability occurs when the articles leave the manufacturer's control and enter into the mainland market. Because of the tax liability, the competitive positions of the mainland and Puerto Rican manufacturers are equalized; without it, the mainland manufacturer would carry an unfair tax burden.

The gasoline tax, on the other hand, is not levied until the time of taxable sale. This may occur immediately after the gasoline enters the United States, or it may occur much later, after the gasoline has passed through the hands of several middlemen producers. The point is that the gasoline has entered the mainland market on equal terms with mainland-manufactured gasoline. For all of Puerto Rico's arguments to the contrary, the difference could hardly be clearer.

V

To sum up, we hold that the cover over provision at issue, 26 U.S.C. § 7652(a)(3) (1976), requires that the Treasury cover over to Puerto Rico only those revenues collected pursuant to the Foraker equalization tax, 26 U.S.C. § 7652(a)(1) (1976). The gasoline tax revenues at issue were not collected pursuant to the equalization tax. Gasoline is not taxed before it enters the market; thus, Puerto Rican manufacturers obtain no competitive advantage over mainland manufacturers on account of the gasoline tax. Rather, the gasoline tax is collected at a later point, when the producer of the gasoline makes a taxable sale to a retailer. Puerto Rican and mainland gasoline, by this time mixed in the market, is taxed equally. The gasoline tax, therefore, never creates an anticompetitive situation such as that envisioned by Congress when it enacted the Foraker equalization tax and cover over provisions. The gasoline tax revenues are not equalization tax revenues, and need not be covered over to the island treasuries.

We are aware that this interpretation is complex, whereas the holding of the District Court had the advantage of simplicity, in theory if not in practice. But the legislative history of the Jones and Foraker Acts reveals Congress's intention that, as new taxes and new situations developed, the equalization tax would be imposed when necessary to equalize the competitive statuses of manufacturers. This is apparent from the open-ended language of the equalization tax provision: in it Congress did not specify which statutes by their terms would require the imposition of a residual equalization tax upon Puerto Rican goods. The Treasury, and occasionally the courts, must be prepared to examine each domestic tax statute individually, with an eye to whether the mandate of equal competition requires application of the Foraker equalization tax. As the Treasury has noted before, in Revenue Ruling 58-554, application of an equalization tax simply is not warranted in the case of gasoline.

VI

Because we reverse the District Court holding on the merits, and hold that neither Puerto Rico nor the Virgin Islands is entitled to revenues from taxes imposed on its gasoline, we pretermit any discussion of the laches, statute of limitations, or sovereign immunity issues addressed by the District Court and by the parties in their briefs. Moreover, because we find that the cover over provision applies only to equalization taxes, and that the taxes on gasoline of Puerto Rican origin are not equalization taxes, we need not consider the Government's contention that the Highway Trust Fund, created pursuant to the Highway Revenue Act of 1956, § 209A, 70 Stat. 374 (the Highway Fund is codified at 23 U.S.C. § 120 note (1976)), implicitly repeals the cover over provision's application to Puerto Rican gasoline. Under our interpretation, these gasoline tax revenues are not diverted from the Highway Trust Fund.

We hereby reverse the District Court grant of partial summary judgment in favor of Puerto Rico in No. 79-1020 and summary judgment in favor of the Virgin Islands in No. 79-1021, and remand with directions to enter judgment in favor of the United States.[34]

It is so ordered.

[34] Shortly after the District Court decisions in the Puerto Rico and Virgin Islands cases, the United States moved in this court for a stay pending appeal. A motions panel of this court denied the motion, instead ordering the United States Treasury to deposit into an interest-bearing escrow account the revenues at issue in these suits. This account was to be maintained, and revenues and interest accumulated, from the time of the District Court orders until one of two events occurred: 1) the institution of a formal cover over policy following an affirmance on the merits, or 2) a final appellate decision reversing the District Court.

On July 23, 1979, the United States moved in this court to modify the orders to eliminate the requirements for payment of interest, and it also requested that this court consider the motion concurrently with a decision on the merits. Because we reverse the District Court judgment and hold that none of these revenues need be covered over, the first stay orders will expire by their own terms when our decision becomes final, and the subsequent motion to modify will be mooted.

APPENDIX B

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

Civil Action No. 75-1035

COMMONWEALTH OF PUERTO RICO, PLAINTIFF,

v.

W. MICHAEL BLUMENTHAL, DEFENDANT.

ORDER

Upon consideration of the parties' cross-motions for summary judgment, the points and authorities filed in support thereof and opposition thereto, the argument of counsel in open Court, the entire record herein, and for the reasons set forth in the Court's Memorandum issued this same day, it is by the Court this 7th day of October, 1978,

ORDERED that plaintiff's motion for summary judgment be, and hereby is, granted in part and denied in part; and it is further

ORDERED that defendant's cross-motion for summary judgment be, and hereby is, denied; and it is further

ORDERED that the defendant Secretary of the Treasury shall rebate to the Treasury of Puerto Rico all federal gasoline excise taxes collected since September 13, 1974 until the present on gasoline refined in Puerto Rico and transported to the United States; and it is further

ORDERED that the defendant Secretary of the Treasury shall cover into the Treasury of Puerto Rico all federal gasoline excise taxes collected in the future on gasoline refined in Puerto Rico and transported to the United States.

/s/ Oliver Gasch

Judge

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UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

Civil Action No. 75-1035

COMMONWEALTH OF PUERTO RICO, *Plaintiff*,

v.

W. MICHAEL BLUMENTHAL, *Defendant*.

MEMORANDUM

Presently before the Court are the parties' cross-motions for summary judgment. Plaintiff, the Commonwealth of Puerto Rico, asserts that it is entitled to a rebate of all gasoline excise taxes that have been levied and collected on gasoline refined in Puerto Rico and transported to the United States. Plaintiff specifically relies on a statutory provision originally enacted as section 9 of the Jones Act,[1] and which provides that "all taxes collected under the internal revenue laws of the United States on articles produced in Puerto Rico and Transported to the United States, or consumed in the island shall be covered into the Treasury of Puerto Rico."[2] Defendant, the Secretary of the Treasury, contends that the foregoing provision was intended to apply only to revenue collected under so-called "equalization" taxes imposed on goods produced in Puerto Rico and transported to the United States. Defendant argues further that the gasoline excise tax, insofar as it applies to gasoline transported to the United States from Puerto Rico, is not an equalization tax. Alternatively, defendant contends that the Federal Aid Highway Act of 1956[3] bars the covering over to Puerto Rico of any revenues from the Gasoline tax.

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[1] 39 Stat. 951 (1917).

[2] 48 U.S.C. § 734 (1970), also codified at 26 U.S.C. § 7652(a)(3) (1976).

[3] 70 Stat. 374 (1956).

The Court, having considered the arguments presented by both parties, and for the reasons discussed below, concludes that the cover over provision requires that taxes collected on Puerto Rican gasoline[4] be covered into the Puerto Rican Treasury. In short, defendant's narrow construction of the cover over provision is contrary to the provision's plain meaning and is not supported by the provision's legislative history. Moreover, defendant's attempt to distinguish the excise tax from the excises on Puerto Rican tobacco and alcohol (the revenues from which are covered into the Puerto Rican Treasury) does not withstand close scrutiny. Nevertheless, the Court concludes that plaintiff's motion for summary judgment should not be granted in its entirety. The Court believes that plaintiff is entitled to a covering over only of those gasoline tax revenues collected on Puerto Rican gasoline since September, 1974, when Puerto Rico first asserted its claim to the Secretary of the Treasury for these tax revenues.

BACKGROUND

A. The Gasoline Excise Tax.

At the outset, it is important to emphasize that the focus of the case at bar is the excise tax imposed on gasoline. This tax was originally enacted in 1932, and its present codification provides that "[t]here is hereby imposed on gasoline sold by the producer or importer thereof, or by any producer of gasoline, a tax of 4 cents a gallon." 26 U.S.C. §4081(a) (1976). The statutory scheme does not define importer, nor does it otherwise specify whether Puerto Rico gasoline is within the scope of the tax. In any event, the tax has been levied on gasoline refined in Puerto Rico and shipped to the United States, and defendant estimates that $350,000,000 of

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[4] Throughout this memorandum, the term "Puerto Rican gasoline" refers to gasoline refined in Puerto Rico and transported to the United States.

revenues have been collected from the tax on Puerto Rican gasoline.[5]

Although the gasoline tax is levied at the time of sale, the tax is clearly a manufacturer's excise tax and not a retail sales tax. The taxing provision provides for the imposition of the tax if the producer or importer consumes the gasoline for his own use and does not sell it. *See* 26 U.S.C. §4082(c) (1976). Moreover, in *Gurley* v. *Rhoden*, 421 U.S. 200 (1975), the Supreme Court, in holding that the incident of the gasoline tax is on the producer (or importer) and not the consumer, recognized that the tax is one on production.

B. *Relevant Tax Provisions Pertaining to Puerto Rico.*

In support of its claim that revenues from the excise on Puerto Rico gasoline should be rebated to the Treasury of Puerto Rico, plaintiff relies on the cover over provision originally enacted in 1917 as section 9 of the Jones Act. To understand the arguments raised by both parties, however, it is necessary to briefly review other tax provisions specifically applicable to Puerto Rico.

The United States originally obtained Puerto Rico in 1899. In 1900, Congress passed the Foraker Act,[6] which established a general taxing scheme for Puerto Rico. The Act provided several sources of revenue for the Puerto Rican Treasury: taxes levied by the permanent government of Puerto Rico, once established, under its own locally applicable internal revenue laws; custom duties imposed on goods entering Puerto Rico from countries other than the United States; and revenue from an equalization tax imposed on goods entering Puerto Rico from the United States. Section 3 of the Foraker Act imposed this equalization tax on goods from the United States going into Puerto Rico, and it

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[5] *See* Statement of Material Facts as to Which Defendant Contends There is no Genuine Issue, ¶ 16. Gasoline has been refined in Puerto Rico and transported to the United States since 1956.

[6] 31 Stat. 77 (1900).

also imposed an equalization tax on goods from Puerto Rico going into the United States. This latter tax was deemed necessary because goods entering the United States from Puerto Rico were subject to neither custom duties imposed on goods imported from foreign countries nor the excise taxes levied on goods manufactured in the United States.[7] Thus, without an equalization tax, Puerto Rican manufacturers who transported their goods to the United States would have a competitive advantage over American manufacturers subject to federal manufacturers excise tax levied in the United States. Section 3 of the Foraker Act was intended to eliminate this competitive gap; it specifically provided that Puerto Rican goods transported to the United States should be subject to a "tax equal to the internal-revenue tax imposed in the United States upon like articles of merchandise of domestic manufacture."[8]

The Foraker Act also provided that the revenue from the equalization tax on goods shipped from Puerto Rico to the United States initially would be held for the benefit of Puerto Rico. This provision expired upon the establishment of the government of Puerto Rico, however, and the revenue from the equalization taxes thereafter went into the general Treasury of the United States.

In 1917, Congress passed the Jones Act, which was primarily intended to give increased rights and governmental powers to Puerto Rico. More importantly for the purposes of the case at bar, section 9 of the Jones Act provided that "all taxes collected under the internal revenue laws of the United States on articles produced in Puerto Rico and transported to the United States, or consumed in the island shall be covered

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[7] Section 3 of the Foraker Act provided that articles should enter Puerto Rico from the United States and the United States from Puerto Rico duty free. Section 14 of the Act provided generally that the internal revenue laws of the United States did not apply in Puerto Rico. *See* 48 U.S.C. §734 (1970).

[8] 26 U.S.C. § 7652(a)(1) (1976).

into the Treasury of Puerto Rico." Congress enacted this cover over provision to compensate for the revenue loss to Puerto Rico resulting from disruption of foreign trade with Puerto Rico during World War I. Historically, Puerto Rico relied on imports from European countries, but the disruption in trade during World War I forced Puerto Rico to rely increasingly on imports from the United States. Because duties on imports from Europe were the primary source of revenue for Puerto Rico, however, and because imports from the United States were made duty free by the Foraker Act, an additional source of revenue for Puerto Rico became necessary. The House Committee Report on the Jones Act stated:

> The loss of this revenue has seriously embarassed the Porto Rican Government, and it is believed to be just and fair that it should receive the internal-revenue taxes collected upon its products, whether those products are used in Porto Rico or produced in Porto Rico and transported to and used in the United States.

H. Rep. 77, 64th Cong., 1st Sess. 1-2 (1916). To make clear the intended broad scope of the cover over provision, the Senate Committee amended it to apply to internal revenue taxes on goods consumed in Pueto Rico but which had been produced elsewhere.[9] Thus, as finally enacted, section 9 provided for the covering over to Puerto Rico of all internal revenue taxes on products either consumed in Puerto Rico or produced in Puerto Rico and transported to the United States.[10]

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[9] *See* S. Rep. 579, 64th Cong., 1st Sess. 2 (1916).

[10] In 1950, the Puerto Rican federal Relations Act was enacted. 64 Stat. 319 (1950). This Act led to the creation of the Commonwealth of Puerto Rico as it now exists. It also continued in force and effect the Jones Act of 1917, which itself had continued in effect the significant tax provisions of the Foraker Act of 1900. Thus, the cover over provision of section 9 of the Jones Act, as well as the equalization tax provision originally contained in section 3 of the Foraker Act on Puerto Rican goods shipped to the United States, have remained in effect to the present.

C. The *Federal Excise Taxes on Tobacco and Alcohol.*

The excise taxes on tobacco and alcohol are relevant to a resolution of the issue before the Court. A considerable amount of tobacco and alcohol produced in Puerto Rico is transported to the United States and subjected to taxation upon shipment into the United States; and, pursuant to section 9 of the Jones Act, the revenue from the excise taxes on Puerto Rican tobacco and alcohol has always been covered into the Puerto Rican Treasury. During 1977, the United States' excise taxes on Puerto Rican rum and Puerto Rican tobacco amounted to approximately $134 million and $9 million, respectively.[11]

The excise tax provision regarding alcohol provides for a tax on "all distilled spirits in bond or produced in or imported into the United States. . . ." 26 U.S.C. § 5001 (1976).[12] The excise tax provision regarding tobacco provides for a tax on cigars, cigarettes and other tobacco products "manufactured in or imported into the United States." 26 U.S.C. §5701 (1976).[13] As discussed in greater length below, defendant contends that the excises on Puerto Rican tobacco and alcohol are levied pursuant to the equalization tax provi-

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[11] *See* Exhibit C to Plaintiff's Opposition to Defendant's Cross-Motion for Summary Judgment.

[12] Section 5001(a)(10) of Title 26, which was not discussed by either of the parties, specifically provides that "[e]xcept as provided in section 5314, upon bay rum, or any article containing distilled spirits, brought from Puerto Rico into the United States for consumption or sale there is hereby imposed a tax on the spirits contained therein at the rate imposed on distilled spirits produced in the United States." This provision was enacted in 1909. *See* 35 Stat. 594.

[13] Again, neither of the parties addressed a subsection of section 5702 pertaining to Puerto Rico. Subsection (b)(1) defines "importer" as "any person in the United States to whom nontaxpaid tobacco products . . . manufactured in a foreign country, Puerto Rico, the Virgin Islands, or a possession of the United States are shipped or consigned . . ."This definitional provision apparently was first enacted in the Revenue Act of 1954.

sion of section 3 of the Foraker Act and not pursuant to sections 5001 and 5701 of the Internal Revenue Code. At the same time, defendant argues that the excise on Puerto Rican gasoline is levied pursuant to section 4081 of the Internal Revenue Code and not pursuant to section 3 of the Foraker Act. This asserted distinction between the excises on Puerto Rican tobacco and alcohol and the excise on Puerto Rican gasoline is critical to defendant's argument that the revenue from the excise on Puerto Rican gasoline is not within the scope of the cover over provision of section 9 of the Jones Act.

MERITS

A. *The Scope of the Cover Over Provision.*

Plaintiff's argument in support of its claim that the revenue from the excise on Puerto Rican gasoline should be covered into the Puerto Rican Treasury is direct in its approach. Plaintiff argues with considerable force that the meaning of the cover over provision is plain on its face and clearly extends to revenues from the excise on Puerto Rican gasoline. Section 9 of the Jones Act, as it is now codified,[14] refers to "*all taxes* collected under *the internal revenue laws of the United States* on articles produced in Puerto Rico and transported to the United States. . ." (Emphasis added.) The provision is all-inclusive in scope; the meaning of the term "all taxes" could not be clearer, and the meaning of the term "the internal revenue laws of the United States" seems equally clear. Without question, the excise levied on Puerto Rican gasoline, like the excises on Puerto Rican tobacco and alcohol, are "taxes collected under the internal revenue laws of the United States." Accordingly, the plain meaning of the provision would appear to require the covering into the Puerto Rican Treasury of all taxes collected on Puerto Rican gasoline.

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[14] *See* 48 U.S.C. § 734; 26 U.S.C. § 7652(a)(3).

In an effort to overcome the cover over provision's plain meaning, defendant presents several arguments, none of which are meritorious. In sum, defendant contends that the meaning of the provision is not clear on its face and the provision's legislative history and historical context indicate that it was intended to provide only for the covering over of revenues collected pursuant to the equalization tax provision of section 3 of the Foraker Act. At the outset, defendant contends that the term "internal revenue laws of the United States" is inherently ambiguous and cannot be presumed to include all internal revenue laws. Yet, in view of the provision's sweeping reference to "all taxes," this argument by defendant is at best a strained one. The inclusion of a second "all" immediately preceding the term "internal revenue laws" would appear unnecessarily repetitive and awkward.

Nevertheless, defendant proceeds to argue that the legislative history of section 9 of the Jones Act, as well as the historical circumstances surrounding the section's enactment, make clear that the cover over provision was intended to encompass only revenue from equalization tax levies. Defendant's reliance on legislative history is noticeably weak, and defendant has not cited any portion of the legislative history directly supporting its narrow construction of the cover over provision. Defendant's only reference to the legislative history of any significance is a quotation from the House Committee Report, as follows:

> It appears that the present rule is to pay into the Porto Rican Treasury those taxes that are collected under the internal-revenue laws of the United States on articles produced and used in Porto Rico, and into the Treasury of the United States internal-revenue taxes collected on articles produced in Porto Rico but transported to the United States. In the opinion of your committee *these taxes* should all be covered into the treasury of Porto Rico.

H. Rep. 77, 64th Cong., 1st Sess. 1-2 (emphasis added by defendant). Defendant concludes that it is clear "that the phrase 'these taxes' as employed in the above passage refers only to revenues from the 'equalization' taxes then being collected on articles produced in Puerto Rico and transported to the United States."[15] In the same manner, defendant relies on the historical circumstances at the time of the enactment of section 9, arguing that because the Foraker Act section 3 equalization taxes were the only taxes remaining in 1917 capable of being covered over to Puerto Rico but not then being covered over, then Congress must have intended to cover over *only* the then-existing equalization taxes on Puerto Rican goods being transported to the United States.

It is clear, however, that defendant is urging a leap in reasoning that is not supported either by the wording of section 9 or by its legislative history. Defendant no doubt is correct in suggesting that Congress, in seeking additional revenue for Puerto Rico, focused on the specific taxes affecting Puerto Rico that were not then being covered into the Puerto Rican Treasury. In 1917, these taxes included the equalization taxes on Puerto Rican goods transported to the United States. But, defendant is asking the Court to read into the broad language of the cover over provision a Congressional intent to exclude from the provision's scope internal revenue taxes different from the equalization taxes and not in existence in 1917. There is no support for such an inference. In fact, the provision itself expressly provides for the covering over of internal revenue taxes that clearly are not equalization taxes, *i.e.*, internal revenue taxes on goods produced and consumed in Puerto Rico. The Senate Committee Report also reflects on intent to make the provision broad enough to include all internal revenue taxes on goods connected with Puerto Rico.[16] Moreover,

[15] Memorandum in Support of Defendant's Cross-motion for Summary Judgment and in Opposition to Plaintiff's motion for Summary Judgment at 9.

[16] *See* note 9 *supra* and accompanying text.

defendant's argument that the provision be interpreted as limited to equalization taxes in effect in 1917 is contrary to the well-established principle that an all-inclusive statutory provision should be presumed to cover persons or things that subsequently fall within its scope. *See, e.g., DeLima* v. *Bidwell*, 182 U.S. 1, 197 (1901). In the face of the broad language of the cover over provision, defendant has failed to show that the excise tax on Puerto Rican gasoline should not be considered within the scope of the provision.

The weakness of defendant's construction of the cover over provision is conclusively demonstrated by the illogic of defendant's asserted distinction between the excises on Puerto Rican tobacco and alcohol and the excise on Puerto Rican gasoline. Consistent with his position that the cover over provision extends only to equalization taxes, defendant argues that the excises on Puerto Rican tobacco and alcohol, but not the excise on Puerto Rican gasoline, are equalization tax levies. In other words, defendant argues that the excises on Puerto Rican tobacco and alcohol are not imposed pursuant to sections 5001 and 5701 of the Internal Revenue Code. This argument fails for two reasons, however. First, both sections 5001 and 5701 appear to contain subsections specifically extending the excise taxes levied by sections 5001 and 5701 to tobacco and alcohol produced in Puerto Rico and transported to the United States.[17]

Secondly, and more importantly, sections 5001 and 5701 like section 4081 (which provides for the gasoline excise tax), each expressly extend to products imported into the United States. Defendant attempts to negative this fact, however, by asserting that goods shipped from Puerto Rico to the United States traditionally have not been considered as "imported into the United States." This tradition allegedly derives from the decision of the Supreme Court in the Insular Cases that goods imported from a foreign country. The Court held that

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[17] *See* notes 12 and 13 *supra*.

Puerto Rico is not a foreign country for purposes of the excise taxes. *See, e.g., Downes* v. *Bidwell*, 182 U.S. 244 (1901). According to defendant, although the term "foreign country" has since been removed from the alcohol and tobacco excise provisions, the reference in the provisions to "imported" goods has been administratively construed as excluding goods from Puerto Rico. Yet, even assuming that such an administrative construction exists and is controlling, defendant completely ignores that the same administrative construction would necessarily apply to the gasoline excise tax provision in section 4081, which also extends to "imported " gasoline. If, as defendant contends, alcohol and tobacco shipped from Puerto Rico to the United States is not "imported" for the purposes of sections 5001 and 5701, then gasoline shipped from Puerto Rico to the United States cannot logically be considered "imported" within the meaning of section 4081. In that event, the excise on Puerto Rican gasoline must be viewed as being levied pursuant to the equalization tax provision of section 3 of the Foraker Act. In attempting to distinguish the excises on Puerto Rican tobacco and alcohol from the excise on Puerto Rican gasoline, defendant has proven too much.

In sum, defendant's limited interpretation of the cover over provision finds no support in, and in fact is contrary to, the provision's language and legislative history. Moreover, defendant's interpretation is premised on a distinction lacking any reasonable basis. Thus, the Court must respect the express language of the cover over provision. As the Supreme Court recently observed,"[i]t is not for us to speculate, much less act, on whether Congress would have altered its stance had the specific events of this case been anticipated." *Tennessee Valley Authority* v. *Hill*, 46 U.S.L.W. 4673, 4682 (June 15, 1978). The plain language of the cover over provision compels the conclusion that the excise tax imposed on gasoline refined in Puerto Rico and transported to the United States be covered into the Treasury of Puerto Rico.

B. *The Federal-Aid Highway Act of 1956.* Defendant alternatively argues that the provisions of the Federal-Aid Highway Act of 1956, 70 Stat. 374 (1956), bars the covering over into the Puerto Rican Treasury of any revenues from the gasoline excise tax. The Federal-Aid Highway Act established a National Highway Trust Fund as a mechanism for federal aid to interstate highway construction. In pertinent part, section 209(c)(1)(A) of the Act provides that:

> There is hereby appropriated to the Trust Fund, out of money in the Treasury not otherwise appropriated, amounts equivalent to the following percentages of the taxes received in the Treasury . . . under the following provisions of the Internal Revenue Code. . .
>
> > (A) 100 percent of taxes received after June 30, 1956, under . . . [section] 4081 (tax on gasoline).

Defendant asserts that the foregoing provision bars the use of gasoline tax revenues for any purpose other than interstate highway construction and the thereby precludes the covering over of any gasoline tax revenues to the Treasury of Puerto Rico.

In short, the language of the Federal-Aid Highway Act simply does not create the bar that defendant asserts it creates. Defendant concedes that the Act does not directly earmark gasoline tax revenues for highway construction; *i.e.*, the monies collected from the gasoline tax are not the direct source of the aid distributed for highway construction. Instead, section 209(c)(1)(A) provides for an appropriation to the Trust Fund "out of money in the Treasury not otherwise appropriated, [an] amount[] equivalent to . . . 100 percent of taxes received" under the tax on gasoline. It is clear from the face of section 209(c)(1)(A) that its terms establish a measure for amounts to be appropriated to the Highway Trust Fund, and do not bar direct appropriations of gasoline tax revenues for purposes other than highway construction.

Thus, although the covering of taxes on Puerto Rican gasoline with the Puerto Rican Treasury might be inconsistent

with the policies underlying the Highway Act, it is not in conflict with the terms of the Act itself. No serious argument can therefore be made that the Highway Act impliedly repealed the statutory provision directing the covering over of taxes on Puerto Rican gasoline. *See Tennessee Valley Authority* v. *Hill*, 46 U.S.L.W. 4673, 4683. In the final analysis, the Highway Act did not alter the directive that " all taxes collected under the internal revenue laws of the United States on articles produced in Puerto Rico and transported to the United States . . . be covered into the Treasury of the United States."

SCOPE OF RELIEF

Plaintiff requests the Court, in the exercise of its equity power, to order the Secretary of Treasury to rebate to the Treasury of Puerto Rico all internal revenue taxes that have been collected on Puerto Rican gasoline shipped to the United States. The Court concludes, however, that because of the significant delay of plaintiff in asserting its claim, such broad retroactive relief is not justified.

The Government of Puerto Rico, without any apparent good cause, waited nearly twenty years to assert its claim that the cover over provision requires that the taxes levied on Puerto Rican gasoline be covered into the Puerto Rican Treasury. The parties agree that the shipment to the United States of gasoline refined in Puerto Rico began in 1956. At that time, both the cover over provision, which had been enacted in 1917, and the gasoline excise tax, which had been enacted in 1932, were in effect. Yet, it appears that plaintiff did not present any claim for the tax revenues collected on Puerto Rican gasoline until September, 1974.[18] There is no evidence that between 1956 and 1974 the government of Puerto Rico lacked either the power or *the knowledge of facts necessary* to assert its claim. At oral hearing, counsel for

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[18] *See* Statement of Material Facts as to Which Plaintiff Contends There is no Genuine Issue, ¶ 9.

plaintiff candidly admitted that he was unable to explain why the Government of Puerto Rico had delayed so long in asserting its claim.

The *delay* by plaintiff in the assertion of its claim is not insignificant. Plaintiff is seeking the rebating of approximately $350,000,000 in tax revenues that have been collected on Puerto Rican gasoline.[19] Moreover, plaintiff does not dispute that since 1956 Puerto Rico has received substantial *benefits from the Trust Fund* established by the Federal-Aid Highway Act.[20] Viewing this situation realistically, it is possible that if Congress had been on notice that Puerto Rico was entitled to the revenue from excise tax on Puerto Rico gasoline, then Congress might have chosen to alter either the scope of the cover over provision or the amount of the appropriations to Puerto Rico from the Highway Trust Fund. Therefore, by having delayed the assertion of its claim to the gasoline tax revenues, Puerto Rico could be receiving a huge windfall if all past taxes collected on Puerto Rico gasoline are rebated to the Puerto Rican Treasury. Given the total absence of any explanation for the eighteen-year delay in the assertion of the claim, the Court believes that an order requiring the Secretary to rebate all past taxes collected on Puerto Rican gasoline would be manifestly unfair. The Court's exercise of its equitable discretion in this manner is consistent with the well-established principle that an equitable claim that is prejudicially untimely is barred by *laches*. Plaintiff cannot be allowed to enforce its claim when it "has inexcusably slept on [its] rights so as to make a decree against the defendant unfair." *Holmberg* v. *Armbrecht*, 327 U.S. 392, 396 (1946).

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[19] *See* note 5 *supra* and accompanying text.

[20] *See* Statement of Material Facts as to Which Defendant Contends There is no Genuine Issue, ¶ 22; Plaintiff's Response to Defendant's Statement of Material Facts as to Which Defendant Contends There is no Genuine Issue, ¶8.

Accordingly, the Court concludes that the Secretary should rebate to the Treasury of Puerto Rico all taxes collected on Puerto Rican gasoline since September 13, 1974 until the present, and the Secretary shall cover into the Puerto Rican Treasury all taxes collected on Puerto Rican gasoline in the future.

/s/ Oliver Gasch

Judge

Date: October 7th, 1978

APPENDIX C

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

September Term, 1980

No. 79-1020

Civil Action No. 75-1035

COMMONWEALTH OF PUERTO RICO

v.

W. MICHAEL BLUMENTHAL, SECRETARY,
DEPARTMENT OF THE TREASURY, *Appellant*

No. 79-1021

Civil Action No. 76-0916

VIRGIN ISLANDS

v.

W. MICHAEL BLUMENTHAL, SECRETARY,
DEPARTMENT OF THE TREASURY, *Appellant*

No. 79-1024

Civil Action No. 75-1035

COMMONWEALTH OF PUERTO RICO, *Appellant*

v.

W. MICHAEL BLUMENTHAL, SECRETARY,
DEPARTMENT OF THE TREASURY

BEFORE: McGowan and Wald, Circuit Judges; Pratt*, United States District Judge for the District of Columbia

Filed December 18, 1980

* Sitting by designation pursuant to Title 28 U.S. Code Section 292(a).

ORDER

On consideration of the petitions for rehearing filed by the Virgin Islands and Commonwealth of Puerto Rico, it is

ORDERED, by the Court, that the aforesaid petitions are denied.

Per Curiam

For the Court:

/s/ George A. Fisher
GEORGE A. FISHER
Clerk

APPENDIX D

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

September Term, 1980

No. 79-1020

Civil Action No. 75-1035

COMMONWEALTH OF PUERTO RICO

v.

W. MICHAEL BLUMENTHAL, SECRETARY,
DEPARTMENT OF THE TREASURY, *Appellant*

No. 79-1021

Civil Action No. 76-0916

VIRGIN ISLANDS

v.

W. MICHAEL BLUMENTHAL, SECRETARY,
DEPARTMENT OF THE TREASURY, *Appellant*

No. 79-1024

Civil Action No. 75-1035

COMMONWEALTH OF PUERTO RICO, *Appellant*

v.

W. MICHAEL BLUMENTHAL, SECRETARY,
DEPARTMENT OF THE TREASURY

BEFORE: Wright, Chief Judge; McGowan, Tamm, Robinson, MacKinnon, Robb, Wilkey, Wald, Mikva and Edwards, Circuit Judges; Pratt*, United States District Judge for the District of Columbia

Filed December 18, 1980

* Sitting by designation pursuant to Title 28 U.S. Code Section 292(a).

ORDER

The suggestions for rehearing *en banc* filed by the Virgin Islands and Commonwealth of Puerto Rico having been transmitted to the full Court and no judge in regular active service, and no member of the panel which considered these cases, having requested a vote with respect thereto, it is

ORDERED, by the Court, *en banc*, that the aforesaid suggestions for rehearing *en banc* are denied.

Per Curiam

For the Court:

/s/ George A. Fisher
GEORGE A. FISHER
Clerk

Circuit Judge Ginsburg did not participate in this order.

APPENDIX E

Internal Revenue Code of 1954 [26 U.S.C.]:

Section 4081 Imposition Of Tax.

(a) *In General.* — There is hereby imposed on gasoline sold by the producer or importer thereof, or by a producer of gasoline, a tax of 4 cents a gallon. . . .

* * *

Section 4082. Definitions.

(a) *Producer.* — As used in this subpart, the term "producer" includes a refiner, compounder, blender, or wholesale distributor, and a dealer selling gasoline exclusively to producers of gasoline, as well as a producer. Any person to whom gasoline is sold tax-free under this subpart shall be considered the producer of such gasoline.

* * *

(c) *Certain Uses Defined as Sales.* — If a producer or importer uses (otherwise than in the production of gasoline or of special fuels referred to in section 4041) gasoline sold to him free of tax, or produced or imported by him, such use shall for the purposes of this chapter be considered a sale.

Section 4083. Exemption Of Sales To Producer.

Under regulations prescribed by the Secretary the tax imposed by section 4081 shall not apply in the case of sales of gasoline to a producer of gasoline.

Section 5001. Imposition, rate, and attachment of tax

(a) *Rate of tax* —

(1) *General.* — There is hereby imposed on all distilled spirits in bond or produced in or imported into the United States an internal revenue tax at the rate of $10.50 on each proof gallon or wine gallon when below proof and a proportionate tax at a like rate on all fractional parts of such proof or wine gallon.

* * *

(10) *Alcoholic compounds from Puerto Rico.* — Except as provided in section 5314, upon bay rum, or any article containing distilled spirits, brought from Puerto Rico into the United States for consumption or sale there is hereby imposed a tax on the spirits contained therein at the rate imposed on distilled spirits produced in the United States.

(b) *Time of attachment on distilled spirits.* — The tax shall attach to distilled spirits as soon as this substance is in existence as such, whether it be subsequently separated as pure or impure spirits, or be immediately, or at any subsequent time, transferred into any other substance, either in the process of original production or by any subsequent process.

* * *

Section 5006. Determination of tax

(a) *Requirements.* —

(1) *General.* — Except as otherwise provided in this section, the internal revenue tax on distilled spirits shall be determined when the spirits are withdrawn from bond.

* * *

(2) *Distilled spirits entered for storage.* —

(A) *Bonding period limitation.* — Except as provided in subparagraph (B), the tax on distilled spirits entered for deposit in storage in internal revenue bond shall be determined within 20 years from the date of original entry for deposit in such storage.

Section 5701. Rate of tax

(a) *Cigars.* — On cigars, manufactured in or imported into the United States, there shall be imposed the following taxes:

(1) *Small cigars.* — On cigars, weighing not more than 3 pounds per thousand, 75 cents per thousand;

(2) *Large cigars.* — On cigars weighing more than 3 pounds per thousand, a tax equal to 8 1/2 percent of the wholesale price, but not more than $20 per thousand.

Cigars not exempt from tax under this chapter which are removed but not intended for sale shall be taxed at the same rate as similar cigars removed for sale. .

(b) *Cigarettes.* — On cigarettes, manufactured in or imported into the United States, there shall be imposed the following taxes:

(1) *Small cigarettes.* — On cigarettes, weighing not more than 3 pounds per thousand, $4 per thousand;

(2) *Large cigarettes.* — On cigarettes, weighing more than 3 pounds per thousand, $8.40 per thousand; except that, if more than 6 1/2 inches in length, they shall be taxable at the rate prescribed for cigarettes weighing not more than 3 pounds per thousand, counting each 2 3/4 inches, or fraction thereof, of the length of each as one cigarette.

* * *

Section 5702. Definitions

When used in this chapter —

* * *

(l) *Importer.* — "Importer" means any person in the United States to whom nontaxpaid tobacco products or cigarette papers or tubes manufactured in a foreign country, Puerto Rico, the Virgin Islands, or a possession of the United States are shipped or consigned; any person who removes cigars or cigarettes for sale or consumption in the United States from a customs bonded manufacturing warehouse; and any person who smuggles or otherwise unlawfully brings tobacco products or cigarette papers or tubes into the United States.

* * *

Section 5703. Liability for tax and method of payment

* * *

(b) *Method of payment of tax.* — The taxes imposed by section 5701 shall be determined at the time of removal of the tobacco products and cigarette papers and tubes.

* * *

Section 7652. Shipments To The United States.

(a) Puerto Rico. —

(1) *Rate of Tax.* — Except as provided in section 5314, articles of merchandise of Puerto Rican manufacture coming into the United States and withdrawn for consumption or sale shall be subject to a tax equal to the internal revenue tax imposed in the United States upon the like articles of merchandise of domestic manufacture.

* * *

(3) *Deposit of internal revenue collections.* — All taxes collected under the internal revenue laws of the United States on articles produced in Puerto Rico and transported to the United States (less the estimated amount necessary for payment of refunds and drawbacks), or consumed in the island, shall be covered into the treasury of Puerto Rico.

31 U.S.C. §725s[b](62):

Section 725s. Same; trust funds

(a) The funds appearing on the books of the Government and listed in subsections (b)[1] and (c) of this section shall be classified on the books of the Treasury as trust funds. All moneys accruing to these funds are hereby appropriated and shall be disbursed in compliance with the terms of the trust.

* * *

(62) Puerto Rico special fund (Internal Revenue).

* * *

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[1] The designation (b) does not appear in this section.

APPENDIX F

Nos. 79-1020, 79-1021, 79-1022 79-1024

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COULUMBIA CIRCUIT

COMMONWEALTH OF PUERTO RICO,
Plaintiff-Appellee-Cross-Appellant

v.

W. MICHAEL BLUMENTHAL, Secretary,
Department of the Treasury,
Defendant-Appellant-Cross-Appellee

VIRGIN ISLANDS,
Plaintiff-Appellee-Cross-Appellant

v.

W. MICHAEL BLUMENTHAL, Secretary,
Department of the Treasury,
Defendant-Appellant-Cross-Appellee

On Appeals From The Orders Of The United States District Court For The District Of Columbia

---

THE SUGGESTION BY THE SECRETARY OF THE TREASURY FOR HEARING *EN BANC*

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IN THE UNITED STATES COURT OF APPEALS
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Nos. 79-1020, 79-1021, 79-1022 79-1024

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On Appeals From The Orders Of The United States District Court For The District Of Columbia

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THE SUGGESTION BY THE SECRETARY OF THE TREASURY FOR HEARING *EN BANC*

To the Honorable Judges of the United States Court of Appeals for the District of Columbia Circuit:

Pursuant to Rule 35 of the Federal Rules of Appellate Procedure, the Secretary of the Treasury, appellant-cross-appellee herein, respectfully suggests that the instant appeals be heard and considered *en banc*.

CONCISE STATEMENT OF ISSUES AND THEIR IMPORTANCE

The instant appeals involve issues of exceptional importance to the United States of America, the Commonwealth of Puerto Rico and the Virgin Islands. We have been informed by the Assistant General Counsel, Department of the Treasury, that the substantive issues involve approximately one billion dollars. Additional millions are being added to this amount each month.

The substantive issue involved in the Puerto Rican case is whether the excise tax collected on gasoline sold in the United States imposed by Sections 4081-4083 of the Internal Revenue Code of 1954 (26 U.S.C.), is, under Section 7652(a)(3) of the 1954 Code, to be covered into the treasury of Puerto Rico insofar as collected since 1956 on gasoline refined in Puerto Rico. The substantive issues involved in the Virgin Islands case are (1) whether the excise tax collected on gasoline sold in the United States, imposed by Sections 4081-4083 of the Internal Revenue Code (26 U.S.C.), is, under Section 7652(b)(3) of the 1954 Code and within the limits of that provision, to be transferred and paid over to the Government of the Virgin Island insofar as collected since 1956 on gasoline refined in Virgin Islands; (2) whether the customs duties collected on goods coming into the United States from the Virgin Islands are to be covered into the treasury of the Virgin Islands under Section 28(a) of the Revised Organic Act of the Virgin Islands, c. 588, 68 Stat. 497;[1] and (3) whether the fees collected since January 31, 1975, under Presidential Proclama-

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[1] In its complaint, the Virgin Islands sought customs duties collected since 1917 on goods coming into the United States from the Virgin Islands. The District court held that the Virgin Islands was entitled since the enactment of the Revised Organic Act of the Virgin Islands in 1954 to customs duties collected on goods coming into the United States from the Virgin Islands. In its opposition (p. 15) to the Secretary's motion for stay filed in this Court, the Virgin Islands claimed to seek only those duties collected in the United States on gasoline and other petroleum products produced in the Virgin Islands. None of these products came into the United States before 1966.

tion 3279, as amended, for licenses to import petroleum products entering the United States from the Virgin Islands are to be covered into the treasury of the Virgin Islands as customs duties under Section 28(a) of the Revised Organic Act of the Virgin Islands.

In addition to the substantive issues, several other issues have been presented. In each case, there are the issues of the application of the six year statute of limitations in 28 U.S.C., Section 2401(a) and the application of the doctrine of sovereign immunity. In the Puerto Rican case, there is the issue of the application of the doctrine of laches.

The District Court held that the Commonwealth of Puerto Rico was entitled to the excise tax collected on the sale in the United States of gasoline refined in Puerto Rico, that the Virgin Islands was entitled to the excise tax collected on the sale in the United States of gasoline refined in the Virgin Islands and to the customs duties collected in the United States on goods coming from the Virgin Islands, that the Virgin Islands was not entitled to the fees collected in the United States for licenses to import petroleum and its derivative products from the Virgin Islands, and that the doctrine of sovereign immuntiy was inapplicable in these cases. Although the issue of the application of the six year statute of limitations was presented to the District Court, it did not address this issue. The District Court held that the claim of Puerto Rico for the gasoline excise taxes collected prior to the presentation of such claim to the Secretary on September 13, 1974 was barred by equitable principles.

The gasoline excise taxes claimed by Puerto Rico and by the Virgin Islands have been paid by the Secretary of the Treasury into the Highway Fund, the Land and Water Conservation Fund, and the Airport and Airway Trust Fund.[2] The resolution as to whom Congress has appropriated those moneys is extremely important to the administration of the

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[2] Section 209(c)(1)(A) of the Highway Revenue Act of 1956, 70 Stat. 374, 387, as amended (23 U.S.C., Sec. 120 Note); Section 2(c)

programs financed by the aforementioned funds and to the administration of the possessions.

Pursuant to this Court's order of February 12, 1979, four cents has been deposited into a special fund with respect to each gallon of gasoline brought into the United States from Puerto Rico since October 10, 1978, and brought into the United States from the Virgin Islands since October 11, 1978. There is no statutory mechanism to determine the amount of tax collected on the sale in the United States of gasoline refined in Puerto Rico or in the Virgin Islands. All sales of gasoline are not subject to tax. This Court's order of February 12, 1979, requires the parties to establish a non-statutory mechanism to make this determination. Such a mechanism will ultimately involve not only the Treasury but will also involve refiners of gasoline in the possessions and those who make sales in this country of gasoline refined in the possessions. Thus, a decision in favor of the possessions will have an effect on the private sector.

The customs duties claimed by the Virgin Islands have been paid into the general fund of the United States Treasury. Pursuant to this Court's order of February 12, 1979, those customs duties collected since October 11, 1978, on petroleum products entering this country from the Virgin Islands have been deposited into a special fund. The ultimate effect of a decision in this case for the Virgin Islands on the customs duties issue will affect the administration of the United States Customs Services. A decision in favor of the Virgin Islands for the oil import license fees will affect the administration of that program by the Department of Energy.

Certainly the issues presented are of "exceptional importance" within the meaning of Rule 35(a)(2), Federal Rules of Appellate Procedure.

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and 201(a), Land and Water Conservation Land Act of 1965, 78 Stat. 897, 899, 904 (16 U.S.C., Sec. 460L-5 and 460L-11; 23 U.S.C., Sec. 120 Note); and Section 208(b)(2), Airport and Airway Reserve Act of 1970, 84 Stat. 219, 250.

Because of the administrative and monetary significance of the issues involved, it is reasonable to assume that any party against whom a three judge panel of this Court rules will petition for a rehearing and file a suggestion for a rehearing *en banc*. An initial *en banc* hearing consequently would serve in the interest of judicial economy.[3]

CONCLUSION

We respectfully suggest that because of the extreme importance of the issues presented and in the interest of judicial economy, the hearing of these cases *en banc* is appropriate.

Wherefore, the Secretary respectfully prays that the suggestion for *en banc* hearing in the first instance be granted in these cases.

Respectfully submitted,

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---

[3] We believe that this application is timely under Rule 14, Local Rules of this Court, because the briefs for the Secretary as appellee in Nos. 79-1022 and 79-1024 are not yet due to be filed. Until those briefs are filed, the Court will not have the views of the Secretary with respect to all issues.

IN THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

Nos. 79-1020 79-1024

COMMONWEALTH OF PUERTO RICO,
Plaintiff-Appellee-Cross-Appellant

v.

W. MICHAEL BLUMENTHAL, Secretary,
Department of the Treasury,
Defendant-Appellant-Cross-Appellee

Nos. 79-1021 79-1022

VIRGIN ISLANDS,
Plaintiff-Appellee-Cross-Appellant

v

W. MICHAEL BLUMENTHAL, Secretary,
Department of the Treasury,
Defendant-Appellant-Cross-Appellee

CERTIFICATE OF SERVICE

It is hereby certified that service of the foregoing suggestion for hearing *en banc* has been made on counsel for the Commonwealth of Puerto Rico and on counsel for the Virgin Islands by mailing three copies thereof to each on this 28th day of June, 1979, in an envelope, with postage prepaid, properly addressed to each as follows:

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APR 7 1981
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In the Supreme Court of the United States

OCTOBER TERM, 1980

COMMONWEALTH OF PUERTO RICO, PETITIONER

v.

DONALD T. REGAN,
SECRETARY, DEPARTMENT OF THE TREASURY

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether Section 7652(a)(3) of the Internal Revenue Code of 1954 (26 U.S.C.) requires that the federal excise tax collected, pursuant to Sections 4081-4083 of the Code, on gasoline sold in the United States be covered into the treasury of Puerto Rico insofar as it is collected on the sale of gasoline refined in Puerto Rico.

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In the Supreme Court of the United States

OCTOBER TERM, 1980

No. 80-1252

COMMONWEALTH OF PUERTO RICO, PETITIONER

v.

DONALD T. REGAN,
SECRETARY, DEPARTMENT OF THE TREASURY

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The memorandum opinion of the district court (Pet. App. 44a-58a) is not yet officially reported. The opinion of the court of appeals (Pet. App. 1a-41a) is not yet officially reported.

JURISDICTION

The judgment of the court of appeals was entered on October 17, 1980. The court denied a timely petition for rehearing with a suggestion for rehearing

en banc on December 18, 1980 (Pet. App. 59a-62a). The petition for a writ of certiorari was filed on January 23, 1981. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATUTES AND REGULATION INVOLVED

The relevant provisions of the Act of Apr. 12, 1900, ch. 191, 31 Stat. 77 (commonly known as the Foraker Act); of the Act of Mar. 2, 1917, ch. 145, 39 Stat. 951 (commonly known as the Jones Act); of Sections 4081, 4082, 4083, 7652 and 7653 of the Internal Revenue Code of 1954 (26 U.S.C.; and of Section 48.4081-1 of the Treasury Regulations on Manufacturers and Retailers Excise Taxes (1954 Code) (26 C.F.R.), are set forth in the App., *infra*, 1a-8a.

STATEMENT

1. In this action brought against the Secretary of the Treasury, petitioner seeks a declaratory judgment that Section 7652(a)(3) of the Internal Revenue Code of 1954 (26 U.S.C.)[1] requires that the excise tax collected, pursuant to the provisions of Sections 4081-4083 of the Code, on the sale in the United States of gasoline refined in Puerto Rico be covered into the treasury of Puerto Rico, and an order compelling the Secretary[2] to cover into the treasury

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[1] In its petition, as well as in the courts below, petitioner has referred primarily not to Section 7652(a)(3) of the 1954 Code, but to the similarly worded proviso in 48 U.S.C. 734. Title 48 of the United States Code has never been enacted into law.

[2] When this action was instituted, the named defendant, then Secretary of the Treasury, was William E. Simon. Pursuant to Fed. R. Civ. P. 25(d), Fed. R. App. P. 43(c), and Rule 40.3 of the Rules of this Court, has successors as Secre-

of Puerto Rico the amount of those taxes previously collected and to be collected in the future on the sale of such gasoline in the United States.[3]

The pertinent facts are undisputed and may be summarized as follows: During the fiscal year 1956-1957, Puerto Rican manufacturers began to refine and ship gasoline to the United States. The sale of this gasoline was subject to a tax that has been levied since 1932 on all gasoline sold by a producer or importer in the United States. Revenue Act of 1932, ch. 209, Section 617, 47 Stat. 266 (now Sections 4081-4083 of the Internal Revenue Code of 1954 (26 U.S.C.)). None of the revenues derived from the tax on the sale in the United States of gasoline refined in Puerto Rico has been covered over to Puerto Rico (Pet. App. 4a).

In correspondence dated September 13, 1974, to the Secretary of the Treasury, petitioner claimed for the first time that both past and future taxes collected under the Internal Revenue Code of 1954 on the sale

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tary of the Treasury have automatically been substituted. References to "respondent" are to the particular Secretary in office at the pertinent time.

[3] A similar claim has been made by the Virgin Islands under Section 7652(b)(3) of the Internal Revenue Code of 1954 in *Virgin Islands* v. *Blumenthal*, Nos. 79-1021 & 79-1022 (D.C. Cir. Oct. 17, 1980), petition for a writ of cert. pending, No. 80-1253. In that case, the Virgin Islands claims that it is entitled under Section 7652(b)(3) of the 1954 Code to the tax collected on the sale in the United States of gasoline refined in the Virgin Islands. The controlling provision of the statute, upon which the Virgin Islands relies, is in all essential respects identical to that upon which petitioner relies (Pet. App. 6a-7a). Unlike petitioner, however, the Virgin Islands also claims the custom duties collected on items coming into the United States from the Virgin Islands.

We are serving a copy of this brief upon counsel for the Virgin Islands in No. 80-1253.

in the United States of gasoline refined in Puerto Rico be covered into the treasury of Puerto Rico. Petitioner grounded this claim upon its construction of Section 7652(a)(3) of the 1954 Code (Pet. App. 4a-5a). In accordance with the opinion of the Office of Legal Counsel, Department of Justice (I-P.R.A. 11, 60-71),[4] the Acting Secretary of the Treasury rejected petitioner's claim on June 10, 1975 (Pet. App. 5a; I-P.R.A. 11, 59). The Acting Secretary concluded that the only taxes to be covered into the treasury of Puerto Rico under Section 7652(a)(3) were, according to its terms, those taxes imposed on certain articles that are "produced in Puerto Rico and transported to the United States";[5] that the only taxes thus imposed were the equalization taxes under Section 7652(a)(1); that the tax imposed by Sections 4081-4083 of the 1954 Code was by virtue of the sale of gasoline in the United States, not by virtue of its production in Puerto Rico and transportation to the United States, and therefore was not to be covered into the treasury of Puerto Rico (I-P.R.A. 60-61).

Following the Secretary's rejection of its claim, petitioner brought this action in the United States District Court for the District of Columbia. In an unpublished order, the district court denied the Secretary's motion to dismiss the complaint on the ground that the court had no jurisdiction to hear the complaint (I-P.R.A. 7, 72, 131).

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[4] "I-P.R.A." and "II-P.R.A." references are respectively to Volumes I and II of the separately bound record appendix filed in the court of appeals.

[5] Section 7652(a)(3) also provides for covering into the treasury of Puerto Rico taxes collected on articles "consumed in the island," but that provision is not involved in this case.

On the merits, the district court held that petitioner was entitled to the excise tax collected on the sale in the United States of gasoline refined in Puerto Rico, but limited petitioner's recovery of the past tax revenues to those collected after September 13, 1974, when petitioner first presented its claim to the Secretary. The district court determined that the terms of Section 7652(a)(3) were all-inclusive so that the taxes to be "covered over" to the treasury of Puerto Rico were not limited to taxes levied under Section 7652(a)(1) of the Code (analogous to the Foraker Act taxes). It was the district court's view that the phrase "produced in Puerto Rico and transported to the United States" in Section 7652(a)(3) was simply a description of certain articles, that all internal revenue taxes of the United States involving such Puerto Rican goods were to be covered into the treasury of Puerto Rico, and that the statute included the tax on the sale in the United States of gasoline refined in Puerto Rico. The district court further found that the tax on gasoline sold was in all respects similar to the liquor and tobacco taxes, the revenues from which have traditionally been covered over to petitioner (Pet. App. 5a-7a, 44a-58a).

In so holding, the district court rejected the Secretary's argument that covering over the gasoline tax was barred by the provisions of the Highway Revenue Act of 1956, ch. 462, Section 209(c)(1)(A), 70 Stat. 398 (23 U.S.C. 120 note), which allocates 100% of the tax collected on the sale of gasoline to the "Highway Trust Fund." Although the district court recognized that its decision might be inconsistent with the policies underlying the Highway Act, it stated that it did not conflict with the terms of the Act. Finally, the district court limited petitioner's recovery to the taxes collected after September 13, 1974, under the doctrine of laches. It concluded that

petitioner had slept on its rights and had thus lulled Congress into thinking that petitioner was not entitled to the gasoline tax under Section 7652(a)(3) (Pet. App. 5a, 7a, 44a-58a).

2. On appeals by both parties, the court of appeals reversed (Pet. App. 1a-41a). It held that petitioner was not entitled under Section 7652(a)(3) to the revenues from the sale in the United States of the gasoline refined in Puerto Rico. Upon examination of the language of the relevant Acts, their legislative history, and the administrative construction of those Acts, the court concluded that the phrase "produced in Puerto Rico and transported to the United States" referred to the events that trigger the imposition of such taxes that are to be covered into the treasury of Puerto Rico. The court of appeals reasoned that any other interpretation would lead to the absurd result of requiring the Secretary to turn over to petitioner the tax (*e.g.*, gift, estate, or sale or other excise tax) on any transaction in the United States in which Puerto Rican goods were involved. The court accordingly concluded that the only taxes to be turned over to petitioner were the equalization taxes imposed by Section 7652(a)(1), and that the tax on the sale of gasoline was not an equalization tax. In so holding, the court did not address the jurisdictional issues of sovereign immunity, the tax exception to the Declaratory Judgment Act, and the statute of limitations, raised by the Secretary's appeal.[6] Moreover, the court found it unnecessary to discuss the issue of laches or the Secretary's

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[6] In view of this action, we have filed a conditional cross-petition on behalf of the Secretary of the Treasury. That petition seeks review by this Court only if it grants Puerto Rico's petition in this case or that of the Virgin Islands (No. 80-1253).

contention with respect to the Highway Revenue Act (Pet. App. 1a-40a).

ARGUMENT

1. The court of appeals correctly held that Section 7652(a)(3) of the Internal Revenue Code of 1954 does not require federal excise taxes collected on gasoline refined in Puerto Rico and sold in the United States to be paid over to the treasury of Puerto Rico.

Section 7652(a)(3) of the Internal Revenue Code of 1954, App., *infra*, 3a, provides that—

> All taxes collected under the internal revenue laws of the United States on articles produced in Puerto Rico and transported to the United States (less the estimated amount necessary for payment of refunds and drawbacks), or consumed in the island, shall be covered into the treasury of Puerto Rico.

Petitioner argues (Pet. 7-10) that the phrase "[a]ll taxes" encompasses the gasoline taxes at issue here. There is no question that the Secretary is required to cover over all the taxes described in Section 7652(a)(3). As the court below properly recognized (Pet. App. 10a), the crucial phrase in Section 7652(a)(3) for purposes of determining which taxes are to be covered into the Treasury of Puerto Rico is "taxes * * * on articles produced in Puerto Rico and transported to the United States." This phrase is, as the court of appeals observed (Pet. App. 10a), ambiguous.[7] The words permit a reading, advanced

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[7] Given the ambiguity of the controlling statute, *TVA* v. *Hill*, 437 U.S. 153 (1978), upon which petitioner relies (Pet. 7-9), is irrelevant. There, the Court observed that "[o]ne would be hard pressed to find a statutory provision whose terms were any plainer than those in § 7 of the Endangered Species Act" (437 U.S. at 173).

by the Secretary, that the taxes to be covered over are those that are imposed because certain articles have been produced in Puerto Rico and transported to the United States, *i.e.*, the equalization taxes imposed by Section 7652(a)(1). The words also permit a reading, advanced by petitioner (Pet. 7-8), that the taxes are on any transaction involving certain described articles, *i.e.*, those produced in Puerto Rico and transported to the United States. After a detailed analysis, the court of appeals concluded that the phrase "taxes * * * on articles produced in Puerto Rico and transported to the United States" meant taxes imposed by virtue of the fact that certain articles are so produced and transported (Pet. App. 10a-11a).

The correctness of the decision below is confirmed by the terms and the history of the related provision set forth in Section 7652(a)(1), App., *infra*, 2a. That statute provides for the imposition of taxes on "articles of merchandise of Puerto Rican manufacture coming into the United States" at the same rate as the taxes "imposed in the United States upon the like articles of merchandise of domestic manufacture." Section 7652(a)(2), App., *infra*, 2a, in turn authorizes the Secretary to allow for payment of these taxes before shipment from Puerto Rico. These two companion provisions clearly indicate an assumption that the taxes will be payable by virtue of the taxed articles' having been "transported to the United States" rather than on account of some subsequent transaction. The taxes imposed on manufacturing a product in Puerto Rico and transporting it to the United States are readily collectible. These are the taxes that the court of appeals correctly held payable to petitioner under Section 7652(a)(3).

If, as petitioner urges (Pet. 7-8), the phrase "on articles produced in Puerto Rico and transported to the United States" is simply a description of certain articles, then the taxes to be covered over are those imposed in the United States on any transaction involving a Puerto Rican article. Under that view, if the transfer of such a Puerto Rican article in the United States results in a gift, estate or sales tax, that tax should, according to petitioner, be covered into the treasury of Puerto Rico. To state such a bizarre conclusion is to refute it. As the court of appeals correctly noted (Pet. App. 9a-10a), "[t]he administrative problems inherent in such a reading of the cover over provision are truly staggering. To effectuate this interpretation, Congress would have to separate Puerto Rican goods from other articles before sale, after sale, and throughout the useful life of the article, or else develop tracing procedures for every type of article that Puerto Rico transports to the United States." [8]

These administrative problems are present with respect to petitioner's claim for the tax on the sale in the United States of gasoline refined in Puerto

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[8] As a simple example, it might be noted that Section 4271 of the Internal Revenue Code of 1954 imposes a tax upon the transportation of property by air. If petitioner's reading of Section 7652(a)(3) were correct, it would be necessary to develop some procedure to determine the origin of the contents of every parcel shipped by air in the United States, so that, if the contents had at any time in the past been produced in Puerto Rico and thereafter been transported to the United States, the tax on that shipment could be covered over to the treasury of Puerto Rico. The parallel problem with respect to goods originating in the Virgin Islands would be present under the reading of Section 7652(b)(3) by the Virgin Islands.

Rico. The operation of Sections 4081-4083, imposing a tax upon the sale of gasoline, is such that the taxable transaction may come about only when a local distributor sells gasoline to a retailer.[9] *Gurley* v. *Rhoden*, 421 U.S. 200 (1975).[10] The statute neither establishes nor suggests any mechanism for identifying the origin of the gasoline transferred at the time of taxable sale. Moreover, the rate of tax has changed from time to time,[11] and the applicable rate is the rate prevailing at the time of the taxable sale.[12] Because there is no mechanism, either by statute or regulation, for establishing the origin of gasoline that

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[9] Section 4081 provides that the importer or producer will pay the tax on the sale of gasoline. Section 4082(a) defines "producer" broadly to include distributors, wholesalers and anyone who buys gasoline tax-free. And Section 4083 provides that sales by importers or producers to other producers shall be exempt from tax. See also exemptions in Sections 4221, 6420, 6421; and Section 48.4083-1, Treasury Regulations on Manufacturers and Retailers Excise Taxes (1954 Code) (26 C.F.R.).

[10] In that case, even the retailer was considered the producer because the retailer had purchased the gasoline free of tax.

[11] The current tax is 4 cents per gallon, with the provision in Section 4081(b) that on or about October 1, 1984, the tax shall be 1½ cents per gallon (26 U.S.C. (Supp. III)). When the Internal Revenue Code of 1954 was enacted, the rate was 2 cents per gallon, with the provision in Section 4081 that on or after April 1, 1955, the rate should be 1½ cents per gallon (26 U.S.C. (1952 ed. Supp. II)). For interim changes, see, *e.g.*, Highway Revenue Act of 1956, ch. 462, Section 205, 70 Stat. 389; Federal-Aid Highway Act of 1961, Pub. L. No. 87-61, Section 201(b), 75 Stat. 123.

[12] Section 48.4081-1(b), Treasury Regulations on Manufacturers and Retailers Excise Taxes (1954 Code) (26 C.F.R.), App., *infra*, 4a.

is the subject of a taxable sale, there is likewise no mechanism for establishing when gasoline of Puerto Rican origin is in fact sold, and hence what amount of tax should, under petitioner's reading, be covered over before and after the time when the rate changes.

In sum, petitioner's claim (Pet. 7-9) that its construction of Section 7652(a)(3) is the only permissible one is refuted by the complementary relationship between that provision and Section 7652(a)(1). The court below was therefore fully justified in concluding that the "taxes" referred to in Section 7652(a)(3) are those equalization taxes imposed because certain articles have been produced in Puerto Rico and transported to the United States.

2. The history of the controlling statute fully supports—indeed requires—the court of appeals' conclusion that Congress intended in Section 7652(a)(3) to cover over only those taxes laid for equalization purposes. These are the taxes imposed by Section 7652(a)(1).

Shortly after Puerto Rico was acquired by the United States,[13] Congress passed the Act of Apr. 12, 1900, ch. 191, 31 Stat. 77 (commonly known as the Foraker or First Organic Act), establishing a civilian government and providing revenues for the island's support. The provisions of the Act establish a significant part of the legislative framework for this case. Congress believed that the excise taxes that then characterized the internal revenue system of the United States[14] would unduly burden the people

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[13] Treaty of Peace between the United States and the Kingdom of Spain, Dec. 10, 1898, Art. II, 30 Stat. 1755.

[14] It was characteristic of all of these excise tax statutes in force on January 1, 1900, and of earlier and later excise

of Puerto Rico (H.R. Rep. No. 249, 56th Cong., 1st Sess. 16 (1900)). Accordingly, Congress provided in Section 14 of the Foraker Act, 31 Stat. 80, App., *infra*, 7a, that "the internal-revenue laws * * * shall not have force and effect in Porto Rico." This would have left manufacturers in the United States, and particularly manufacturers of alcohol and tobacco products who were subject to substantial excise taxes [15] on manufacture, vulnerable to tax-free competition from Puerto Rico (Pet. App. 12a-13a). In order to avoid such a result, Congress provided in Section 3 of the Foraker Act, 31 Stat. 77, App., *infra*, 4a-6a, that articles manufactured in Puerto Rico and brought to the United States should be subject to tax at the rate applicable to like articles manufactured in the United

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statutes prior to the Revenue Act of 1917, ch. 63, 40 Stat. 300, that the tax was stated to be on a named article "manufactured," "manufactured and sold," "distilled," "brewed or manufactured and sold," "imported from foreign countries," etc. See, *e.g.*, *Internal Revenue Laws in Force January 1, 1900*, Treas. Dep't Doc. No. 2157 (1900). The War Excise Taxes imposed by Title VI of the Revenue Act of 1917, 40 Stat. 316 *et seq.*, appear to be the first upon the sale of named articles, *e.g.*, upon automobiles, phonographs, jewelry, perfumes, etc., "sold by the manufacturer, producer, or importer" (Section 600, 40 Stat. 316).

[15] At that time, taxes were imposed, for example, on spirits distilled in the United States (Act of Aug. 27, 1894, ch. 349, Section 48, 28 Stat. 563), on tobacco manufactured and sold (Rev. Stat., Section 3368, as amended by the Act of Oct. 1, 1890, ch. 1244, Section 31, 26 Stat. 619, and by the Act of June 13, 1898, ch. 488, Section 3, 30 Stat. 449), and on tobacco imported from foreign countries (Rev. Stat., Section 3377, as amended by the Act of Mar. 1, 1879, ch. 125, Section 14, 20 Stat. 343). Puerto Rico was no longer a foreign country. *DeLima* v. *Bidwell*, 182 U.S. 1, 181-200 (1901); *Downes* v. *Bidwell*, 182 U.S. 244, 248-249 (1901).

States.[16] That provision remains, and now appears as Section 7652(a)(1) of the 1954 Code. Until the local Puerto Rican government was established by Presidential Proclamation,[17] the proceeds of that tax were set aside for use for the benefit of Puerto Rico. But after that government was established, those proceeds were paid into the general fund of the Treasury (Section 4 of the Foraker Act, 31 Stat. 78, App., *infra*, 6a-7a).

It is clear, as the court of appeals pointed out (Pet. App. 15a), that Section 3 of the Foraker Act (now Section 7652(a)(1) of the 1954 Code) "impos[es] an equalization tax, as a condition of entry into the mainland market, on any Puerto Rican article that has escaped a tax previously laid on comparable American-made articles. Only when tax equalization function is needed does the Foraker provision come into play. Furthermore, * * * only domestic taxes on manufacture [*e.g.*, taxes on alcohol distilled and tobacco manufactured] require such equalization. Any tax that applies equally to Puerto Rican and mainland goods, such as a tax on sale, does not require the application of a 'mirror-like' equalization tax."

In 1917, when the customs revenues of Puerto Rico sharply declined because Europe was at war, and

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[16] In Section 3, Congress also provided that articles manufactured in the United States and brought into Puerto Rico should be subject to tax at the rate applicable to like articles manufactured in Puerto Rico. That provision is the predecessor of Section 7653(a)(1) of the Internal Revenue Code of 1954, App., *infra*, 3a. The amounts collected in Puerto Rico under that part of the Foraker Act were paid into the treasury of Puerto Rico after the Proclamation of the President referred to at note 17, *infra*.

[17] The Proclamation (No. 8) was made on July 25, 1901. 32 Stat. 1983.

the Puerto Rican government was in need of added revenues, Congress enacted Section 9 of the Act of Mar. 2, 1917, ch. 145, 39 Stat. 954 (commonly known as the Jones Act or Second Organic Act). That statute is now codified in Section 7652(a)(3). As the court below observed (Pet. App. 16a-23a), the legislative history of Section 7652(a)(3) demonstrates that the taxes to be covered over by this section were the Foraker Act equalization taxes. The House Committee on Insular Affairs stated in pertinent part (H.R. Rep. No. 77, 64th Cong., 1st Sess. 1-2 (1916); emphasis added) that "the present rule is to pay * * * into the Treasury of the United States internal-revenue taxes collected on articles produced in Porto Rico but transported to the United States. In the opinion of your committee *these taxes* should all be covered into the treasury of Porto Rico." The Senate made the covering over provision of the Jones Act coextensive with the Foraker Act by adding the phrase "consumed in the island" (S. Rep. No. 579, 64th Cong., 1st Sess. 2 (1916)).[18] Contrary to petitioner's claim (Pet. 10 n.10), this phrase referred only to the taxes imposed on United States manufactured goods entering Puerto Rico (now Section 7653(a) of the 1954 Code). Petitioner has pointed to no other internal revenue tax relating to Puerto Rico other than the Foraker Act taxes. Indeed, the first part of Section 9 of the Jones Act made the internal revenue laws of the United States inapplicable to Puerto Rico.

3. Petitioner further challenges (Pet. 11-12) the court of appeals' conclusion (Pet. App. 27a-33a) that the administrative construction of the statute by the Treasury is entitled to great weight. But the

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[18] Of course, as petitioner points out (Pet. 10), the Senate made the covering-over provision "all inclusive," *i.e.*, all-inclusive for the Foraker Act taxes (S. Rep. No. 579, *supra*, at 2).

Treasury has been charged with the collection of the taxes under Section 3 of the Foraker Act and its successors, as well as other excises, and with the payment of funds under Section 9 of the Jones Act and its successors in the 1939 and 1954 Codes. As the court below correctly noted (Pet. App. 28a-30a), the Treasury has consistently interpreted the controlling provision (Section 7652(a)(3) or its predecessors), for more than half a century, to require the covering over of only equalization (Foraker Act) taxes; and taxes, such as the gasoline tax, on sales at wholesale or retail are not equalization (Foraker Act) taxes. Congress was aware of this administrative interpretation. See Rev. Rul. 58-554, 1958-2 Cum. Bull. 909, which spells out in detail the administrative interpretation of the Foraker equalization tax provision (Section 7652(a)(1) of the 1954 Code). Indeed, until this case, petitioner has never challenged the Treasury's interpretation. In these circumstances, the Treasury's consistent and longstanding construction should be accorded substantial deference. *Zenith Radio Corp.* v. *United States*, 437 U.S. 443, 450 (1978); *Saxbe* v. *Bustos*, 419 U.S. 65, 74 (1974). See also *Central Tablet Manufacturing Co.* v. *United States*, 417 U.S. 673, 689-690 (1974).

The fact that the Secretary asserted claims of privilege with respect to certain documents requested by petitioner does not, as petitioner argues (Pet. 11-12), undermine the deference to be accorded the Treasury's administrative construction of the statute.[19] The

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[19] The only document cited by petitioner (Pet. 12 n.13) as showing an inconsistent administrative practice is an

district court determined that the documents were within the claimed privileges (I-P.R.A. 156). Petitioner did not appeal this determination and makes no claim that the district court erred. If a document is privileged, the weight of authority is that no inference is to be drawn against the party asserting the privilege. Otherwise the rationale behind allowing the privilege would be destroyed. *Griffin* v. *California*, 380 U.S. 609, 614 (1965); 2 J. Wigmore, *Evidence* § 291(3)(2), at 225 (Chadbourn rev. 1979); *McCormick on Evidence* § 76 (2d ed. 1972). Indeed, the McCormick treatise states that where, as here, the government is the defendant, "an adverse finding cannot be rendered against it as the price of asserting an evidentiary privilege. This is not one of the terms upon which Congress has consented that the United States be subject to liability." *McCormick on Evidence, supra*, § 109, at 234.[20]

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otherwise unidentified memorandum referred to in the course of an extensive Treasury memorandum on S. 1014, 80th Cong., 1st Sess. (1947) (II-P.R.A. 360-364). But this unidentified document does not assist petitioner. It does indicate that some unidentified person in the Miscellaneous Tax Unit gave Section 3360(c) of the 1939 Code (26 U.S.C. (1952 ed.)) (now Section 7652(a)(3) of the 1954 Code) the reading that would require covering over to petitioner retail sales taxes, and presumably gift, estate and income taxes if they arose by virtue of transfers or other transactions involving articles of Puerto Rican origin. These are consequences that petitioner acknowledged to be "absurd" in its brief in the court of appeals (at 5 n.7), and they were firmly rejected by the Secretary as well. See the O'Connell letter, referred to by the court below (Pet. App. 28a-30a) for the views expressed by the Treasury to the Senate with respect to S. 1014.

[20] Fed. R. Civ. P. 26(b)(1) provides that privileged documents are not subject to discovery. The cases cited by petitioner (Pet. 12) are inapposite. In *Washington* v. *Cameron*, 411 F.2d 705 (D.C. Cir. 1969), and in *Illinois State*

4. a. Petitioner also argues (Pet. 12-17) that the tax imposed on "gasoline sold" in the United States is a tax on manufacturing and not a tax on sale and that the only manner in which gasoline coming from Puerto Rico may be subject to tax is under Section 7652(a)(1) of the Code. But, as the court below correctly stated (Pet. App. 36a), "[t]he crucial inquiry is whether the gasoline tax is laid on the act of sale or manufacture." The tax imposed by Section 4081 is on the sale of gasoline, not on its manufacture or refinement. Indeed, this Court in *Gurley* v. *Rhoden*, *supra*, 421 U.S. at 205, recognized that the tax was upon "gasoline sold." There, the Court stated that the gasoline tax was levied on the sale by a person who had purchased the gasoline tax-free.

This Court has also considered similar statutory language to be a tax on sales, and not on manufacturing. *Indian Motocycle Co.* v. *United States*, 283 U.S. 570, 574 (1931). See also, *Import Wholesalers Corp.* v. *United States*, 368 F.2d 577 (Ct. Cl. 1966); *Jacobs Equipment Co.* v. *United States*, 574 F.2d 1040 (10th Cir. 1978); *United States* v. *Stowe-Woodward, Inc.*, 306 F.2d 678, 679 (1st Cir. 1962), cert. denied, 371 U.S. 949 (1963). Likewise, Section 48.4081-1(a), Treasury Regulations on Manufacturers and Retailers Excise Taxes (1954 Code)

Employees Union Council 34 v. *Lewis*, 473 F.2d 561 (7th Cir. 1972), cert. denied, 410 U.S. 928, 943 (1973), the issue was whether the district court should have granted summary judgment without considering the interrogatories propounded, but not yet answered. Here, on the other hand, the Secretary answered the interrogatories and withheld only those records or portions thereof that the district court determined to be privileged.

(26 C.F.R.), App., *infra*, 3a, provides that "Section 4081 imposes a tax on the sale of gasoline * * *."[21]

When Congress has placed a tax on manufacturing or production, it has consistently done so in the Internal Revenue Code and in earlier excise tax statutes by using those precise terms.[22] The statute in *Liggett & Myers Tobacco Co.* v. *United States*, 299 U.S. 383, 384 (1937), upon which petitioner relies (Pet. 16), is accordingly distinguishable. There, the tax was imposed "[u]pon all tobacco and snuff manufactured in or imported into the United States, and hereafter sold by the manufacturer or importer, or removed for consumption or sale * * *." The Court held that the tax was on the manufacturing of tobacco and snuff and not on their sale because, *inter alia*, the tax was based upon each pound of tobacco manufactured regardless of the price obtained upon sale.[23] Whether or not a tax is measured by a percentage of price may help resolve a problem of statutory inter-

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[21] Section 4082(c) of the 1954 Code, App., *infra*, 1a, provides that use of gasoline by the producer or importer is deemed a sale.

[22] See, *e.g.*, tax "on all distilled spirits * * * produced" (Section 5001 of the 1954 Code) or tax "[o]n cigars * * * manufactured" (Section 5701 of the 1954 Code). See also notes 14 & 15, *supra*. Indeed, from the beginning, Congress employed a similar style. Section 15 of the Act of Mar. 3, 1791, ch. 15, 1 Stat. 203, had imposed a tax "upon all spirits * * * distilled within the United States." This excise was repealed by the Act of Apr. 6, 1802, ch. 19, 2 Stat. 148. Thus, a tax on a given article sold is a tax on sale. Petitioner ignores this consistent stylistic pattern used by Congress with respect to the tax laws.

[23] The Court noted that the terms "hereafter sold" or "removed for consumption or sale" marked only the time when the tax was payable (299 U.S. at 386).

pretation when the statute imposes a tax upon an item manufactured and sold, but such a criterion is irrelevant when the statute imposes a tax only on the sale. The manner in which the tax is computed cannot make it a tax on manufacture unless the statute clearly imposes the tax upon the manufacture of a product. The tax under Section 4081 is upon "gasoline sold" and there is nothing in the statute or its legislative history to suggest that the imposition of the tax is on any activity other than its sale.[24] Contrary to petitioner's argument (Pet. 15-17), *Liggett & Myers Tobacco Co.* does not conflict with the decision below. As the court below correctly recognized (Pet. App. 36a-37a), the fact that the tax is imposed upon a sale by the manufacturer or somewhere between the manufacturer and retailer, and is not imposed upon retail sales as such, does not make it any less of a tax on sales. In sum, petitioner's attempt to convert the tax imposed by Sections 4081-4083 on the sale of gasoline into a tax on the refining of gasoline is refuted by the language and operation of the statute.

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[24] The difference between a tax on a product "sold" by the manufacturer, producer, or importer, and a tax on a product "manufactured" rises to constitutional dimensions in at least one context. When the tax on "baseball bats, * * * balls of all kinds, including baseballs * * * sold by the manufacturer" (40 Stat. 316-317) was applied to a shipment of baseballs and bats by the manufacturer to a buyer in Venezuela, this Court in *Spalding & Bros.* v. *Edwards*, 262 U.S. 66, 67 (1923), held that the tax as thus applied violated Art. I, Sec. 9, cl. 5, of the Constitution, providing that "No Tax or Duty shall be laid on Articles exported from any State." On the other hand, when the tax was not on sale, but was on "all filled cheese which shall be manufactured" (Act of June 6, 1896, ch. 337, Section 9, 29 Stat. 255), the tax was upheld even though the filled cheese was manufactured under contract for export. *Cornell* v. *Coyne*, 192 U.S. 418 (1904); cf. *Turpin* v. *Burgess*, 117 U.S. 504 (1886).

b. Petitioner also argues (Pet. 13-14) that under the decision below, gasoline refined in Puerto Rico and transported to the United States will escape taxation. But petitioner ignores the well settled judicial interpretation of the phrase "manufacturer, producer or importer" under the statutes imposing a tax on the sale to be a shorthand expression for first sale in the United States. *Indian Motocycle Co.* v. *United States*, *supra*, 283 U.S. at 574; *United States* v. *Stowe-Woodward, Inc.*, *supra*, 306 F.2d at 679. Here, the term "producer" is defined so broadly in Section 4082(a) as to preclude the possibility that the sale in the United States of Puerto Rican refined gasoline could go untaxed.[25]

The historical relationship between the taxes on tobacco manufactured or imported and on spirits distilled or imported, on the one hand, and the Foraker Act equalization taxes (Section 7652(a)(1) of the 1954 Code), on the other, indicates that the taxes imposed on tobacco and liquor manufactured in Puerto Rico and transported to the United States have consistently been taxes under the Foraker Act equalization tax provisions. As we have noted (*supra*,

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[25] As this Court pointed out in *Gurley* v. *Rhoden*, *supra*, 421 U.S. at 205, Section 4082(a) defines "producer" to include, *inter alia*, "[a]ny person to whom gasoline is sold tax-free." In that case the producer was the operator of several gasoline stations. "Importer" includes "any person who withdraws gasoline from a customs bonded warehouse for sale or use in the United States" (Section 48.4082-1(d) of the Treasury Regulations on Manufacturers and Retailers Excise Taxes (1954 Code) (26 C.F.R.)). Any use of gasoline other than in further production is defined as a sale in Section 4082(c) of the 1954 Code.

It is clear that Congress intended the predecessors of Section 4081(a) to reach the sale of gasoline in the United States by any person making a taxable sale. See 75 Cong. Rec. 7037, 7320 (1932).

pages 11-13), the Foraker Act equalization taxes were enacted because the taxes on tobacco and distilled spirits were on manufacture or on importation from a foreign country. Puerto Rico, however, was no longer a foreign country.[26] Although the taxes on tobacco and distilled spirits are now on their manufacture or on their importation into the United States (Sections 5001(a) and 5701(a) of 1954 Code), Congress has continued to treat the taxes on spirits distilled and tobacco products manufactured in Puerto Rico and transported to this country as being imposed by Section 7652(a)(1). See the amendments made by Section 808 of the Excise Tax Reduction Act of 1965, Pub. L. No. 89-44, 79 Stat. 164, and by Section 1905(a)(2) of the Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1818. Indeed, with respect to the latter amendment, the Senate Finance Committee Report explained (S. Rep. No. 94-938, 94th Cong., 2d Sess. 529 (1976): "Puerto Rico and Virgin Island spirits are taxed separately (under [Section] 7652) [rather than under Section 5001]."[27] In light of this historical devel-

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[26] See *Hooven & Allison Co.* v. *Evatt*, 324 U.S. 652, 669-670 (1945).

[27] Imports from other areas do not cause a tax to be covered into the treasury of Puerto Rico. If tobacco and distilled spirits coming from Puerto Rico are taxed only because they are imports under Sections 5001(a)(1) and 5701, and not because they were produced in Puerto Rico, then the Treasury has been paying too much money to Puerto Rico under Section 7652(a)(3). But this case does not involve the question whether payments have been excessive. The significant matter in this case, as the court below recognized, is that gasoline is taxed because it is "sold," and the tax on sale applies whether the gasoline is refined domestically, in Puerto Rico, or in a foreign country.

opment, there simply is no relevant connection for purposes of this case between the terms "imported" as used in Sections 5001 and 5701 and the term "importer" as used in Section 4081(a).

5. Admittedly, this case involves a substantial amount of money—almost $500 million to date. But the court of appeals' approval of the more-than-half-century interpretation of Section 7652(a)(3) of the Code by the Treasury settles the matter and eliminates the manifold administrative problems created by the district court's decision. For example, the gasoline taxes claimed by petitioner had, prior to the entry of the district court's judgment, been paid by the Secretary into the "Highway Trust Fund," the "Land and Water Conservation Fund", and the "Airport and Airway Trust Fund."[28] Under the de-

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[28] Section 209(c)(1)(A) of the Highway Revenue Act of 1956, ch. 462, 70 Stat. 398, as amended (23 U.S.C. 120 note), appropriated to the Highway Trust Fund "100 percent of the taxes received after June 30, 1956, under * * * [Section] 4081 (tax on gasoline) * * *." Sections 2(c), 201(a) and 202(a) of the Land and Water Conservation Fund Act of 1965, Pub. L. No. 88-578, 78 Stat. 899, 904 (16 U.S.C. 460*l*-5 and 460*l*-11, 23 U.S.C. 120 note), provided for crediting to the land and water conservation fund amounts collected under Section 4081 of the Internal Revenue Code on gasoline sold for use in motorboats and modified Section 209 of Highway Revenue Act of 1956, 70 Stat. 397, accordingly. Section 208(b)(2) of the Airport and Airway Development Act of 1970, Pub. L. No. 91-258, 84 Stat. 250, appropriated the taxes received in the Treasury after June 30, 1970, under Section 4081 of the Internal Revenue Code of 1954, with respect to gasoline used in aircraft, to the Airport and Airway Trust Fund. Section 208(g) of the Act, 84 Stat. 252, modified Section 209(c) of the Highway Revenue Act of 1956 to this end. In *Gurley* v. *Rhoden*, *supra*, 421 U.S. at 206, this Court recognized that the proceeds of the gasoline tax "go not into the

cision below, these gasoline tax revenues are not diverted from the various funds to which Congress intended them to be paid.

Contrary to petitioner's further claim (Pet. 7), the decision below in no way alters the relationship between the United States and Puerto Rico. Indeed, that decision continues the longstanding relationship confirmed by the administrative construction of the statute for more than half a century. The Act of July 3, 1950, ch. 446, 64 Stat. 319 (the Puerto Rican Federal Relations Act of 1950), cited by petitioner (Pet. 7), provides neither support for its claim nor a reason for review of the judgment below. Because of that Act, Congress has normally sought petitioner's approval with respect to legislation applicable to events in Puerto Rico. But Congress apparently neither sought nor obtained petitioner's consent prior to enactment of Section 808 of the Excise Tax Reduction Act of 1965, Pub. L. No. 89-44, 79 Stat. 164, and Section 1905(a)(2) of the Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1818.[29]

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general treasury, but into a special fund used to defray the cost of the federal highway system * * *." And in *Massachusetts* v. *United States*, 435 U.S. 444, 448 (1978), the Court recognized that Congress had provided that the user taxes, which include the gasoline sold for use in aircraft, are paid into the Airport and Airway Trust Fund. Petitioner is entitled to distributions from these funds, but made no contributions thereto. As of September 13, 1974, petitioner had received approximately $250,000,000 from the Highway Trust Fund (II-P.R.A. 214), and nearly $10,000,000 from the other funds.

[29] Apart from its irrelevancy, petitioner's claim (Pet. 7 n.6) that the Act of July 3, 1950, *supra*, cannot be unilaterally

CONCLUSION

For the reasons stated, the petition for a writ of certiorari should be denied.

Respectfully submitted.

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APRIL 1981

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changed by the United States is incorrect. That Act, like any other act or treaty, is not binding on a subsequent Congress. *Clark* v. *Allen*, 331 U.S. 503, 509 (1947); *Whitney* v. *Robertson*, 124 U.S. 190, 194 (1888); *The Chinese Exclusion Case*, 130 U.S. 581, 600 (1889).

APPENDIX

Internal Revenue Code of 1954 (26 U.S.C.):

SEC. 4081. IMPOSITION OF TAX.

(a) *In general.* [as amended by Section 201(b), Federal-Aid Highway Act of 1961, Pub. L. No. 87-61, 75 Stat. 123]—There is hereby imposed on gasoline sold by the producer or importer thereof, or by any producer of gasoline a tax of 4 cents a gallon.

* * * * *

SEC. 4082. DEFINITIONS.

(a) *Producer.* [as amended by Section 201(e)(1), Federal-Aid Highway Act of 1959, Pub. L. No. 86-342, 73 Stat. 615]—As used in this subpart, the term "producer" includes a refiner, compounder, blender, or wholesale distributor, and a dealer selling gasoline exclusively to producers of gasoline, as well as a producer. Any person to whom gasoline is sold tax-free under this subpart shall be considered the producer of such gasoline.

* * * * *

(c) *Certain uses defined as sales.* [as amended by Section 205(c)(6), Airport and Airway Revenue Act of 1970, Pub. L. No. 91-258, 84 Stat. 242]—If a producer or importer uses (other wise than in the production of gasoline or of special fuels referred to in section 4041) gasoline sold to him free of tax, or produced or imported by him, such use shall for the purposes of this chapter be considered a sale.

* * * * *

SEC. 4083. [as amended by Section 1906(b)(13)(A), Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1834] EXEMPTION OF SALES TO PRODUCER.

Under regulations prescribed by the Secretary the tax imposed by section 4081 shall not apply in the case of sales of gasoline to a producer of gasoline.

SEC. 7652. SHIPMENTS TO THE UNITED STATES.

(a) *Puerto Rico.*—

(1) *Rate of tax.* [as amended by Section 204(17), Excise Tax Technical Changes Act of 1958, Pub. L. No. 85-859, 72 Stat. 1430]—Except as provided in section 5314, articles of merchandise of Puerto Rican manufacture coming into the United States and withdrawn for consumption or sale shall be subject to a tax equal to the internal revenue tax imposed in the United States upon the like articles of merchandise of domestic manufacture.

(2) *Payment of tax.* [as amended by Section 1906(b)(13)(A), Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1834]—The Secretary shall by regulations prescribe the mode and time for payment and collection of the tax described in paragraph (1), including any discretionary method described in section 6302(b) and (c). Such regulations shall authorize the payment of such tax before shipment from Puerto Rico, and the provisions of section 7651(2)(B) shall be applicable to the payment and collection of such tax in Puerto Rico.

(3) *Deposit of internal revenue collections.* [as amended by Section 808(b)(3), Excise Tax Reduction Act of 1965, Pub. L. No. 89-44, 79 Stat. 164]—All taxes collected under the internal revenue laws of the United States on articles produced in Puerto Rico and transported to the United States (less the estimated amount necessary for payment of refunds and drawbacks), or consumed in the island, shall be covered into the treasury of Puerto Rico.

* * * * *

SEC. 7653. SHIPMENTS FROM THE UNITED STATES.

(a) *Tax Imposed.*—

(1) *Puerto rico.*—All articles of merchandise of United States manufacture coming into Puerto Rico shall be entered at the port of entry upon payment of a tax equal in rate and amount to the internal revenue tax imposed in Puerto Rico upon the like articles of Puerto Rican manufacture.

(2) *Virgin Islands.*—There shall be imposed in the Virgin Islands upon articles imported from the United States a tax equal to the internal revenue tax imposed in such islands upon like articles there manufactured.

* * * * *

Treasury Regulations on Manufacturers and Retailers Excise Taxes (1954 Code) (26 C.F.R.):

§ 48.4081-1 *Imposition and rates of tax.*

(a) *In general.* Section 4081 imposes a tax on the sale of gasoline by the producer or importer thereof, or by any producer of gasoline,

regardless of when or whether such gasoline was produced by him. For the requirement that producers and importers of gasoline be registered and give bond, see section 4101 and the regulations thereunder. See section 4082(c) and paragraph (c) of § 48.4082-1 for certain uses of gasoline that shall be considered sales of gasoline.

(b) *Rate of tax.* Tax is imposed on the sale of gasoline at the rate applicable on the date on which the gasoline is sold. Following are the rates in effect on or after January 1, 1959:

Gasoline sold	Cents per gallon
(1) January 1, 1959, to September 30, 1959, inclusive	3
(2) October 1, 1959, to September 30, 1972, inclusive	4
(3) On or after October 1, 1972	1½

(c) *Liability for tax.* The tax imposed by section 4081 is payable by the producer or importer making the sale of the gasoline.

Act of Apr. 12, 1900, ch. 191, 31 Stat. 77 *et seq.*:

* * * * *

SEC. 3. That on and after the passage of this Act all merchandise coming into the United States from Porto Rico and coming into Porto Rico from the United States shall be entered at the several ports of entry upon payment of fifteen per centum of the duties which are required to be levied, collected, and paid upon like articles of merchandise imported from foreign countries; and in addition thereto upon articles of merchandise of Porto Rican manufacture coming into the United States and withdrawn for consumption or sale upon payment of a tax equal to the internal-revenue tax imposed in the United States upon the like articles of merchandise of

domestic manufacture; such tax to be paid by internal-revenue stamp or stamps to be purchased and provided by the Commissioner of Internal Revenue and to be procured from the collector of internal revenue at or most convenient to the port of entry of said merchandise in the United States, and to be affixed under such regulations as the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, shall prescribe; and on all articles of merchandise of United States manufacture coming into Porto Rico in addition to the duty above provided upon payment of a tax equal in rate and amount to the internal-revenue tax imposed in Porto Rico upon the like articles of Porto Rican manufacture: *Provided*, That on and after the date when this Act shall take effect, all merchandise and articles, except coffee, not dutiable under the tariff laws of the United States, and all merchandise and articles entered in Porto Rico free of duty under orders heretofore made by the Secretary of War, shall be admitted into the several ports thereof, when imported from the United States, free of duty, all laws or parts of laws to the contrary notwithstanding; and whenever the legislative assembly of Porto Rico shall have enacted and put into operation a system of local taxation to meet the necessities of the government of Porto Rico, by this Act established, and shall by resolution duly passed so notify the President, he shall make proclamation thereof, and thereupon all tariff duties on merchandise and articles going into Porto Rico from the United States or coming into the United States from Porto Rico shall cease, and from and after such date all such merchan-

dise and articles shall be entered at the several ports of entry free of duty; and in no event shall any duties be collected after the first day of March, nineteen hundred and two, on merchandise and articles going into Porto Rico from the United States or coming into the United States from Porto Rico.

SEC. 4. That the duties and taxes collected in Porto Rico in pursuance of this Act, less the cost of collecting the same, and the gross amount of all collections of duties and taxes in the United States upon articles of merchandise coming from Porto Rico, shall not be covered into the general fund of the Treasury, but shall be held as a separate fund, and shall be placed at the disposal of the President to be used for the government and benefit of Porto Rico until the government of Porto Rico herein provided for shall have been organized, when all moneys theretofore collected under the provisions hereof, then unexpended, shall be transferred to the local treasury of Porto Rico, and the Secretary of the Treasury shall designate the several ports and subports of entry in Porto Rico and shall make such rules and regulations and appoint such agents as may be necessary to collect the duties and taxes authorized to be levied, collected, and paid in Porto Rico by the provisions of this Act, and he shall fix the compensation and provide for the payment thereof of all such officers, agents, and assistants as he may find it necessary to employ to carry out the provisions hereof: *Provided, however*, That as soon as a civil government for Porto Rico shall have been organized in accordance with the provisions of this Act and notice thereof shall have been given to the Pres-

ident he shall make proclamation thereof, and thereafter all collections of duties and taxes in Porto Rico under the provisions of this Act shall be paid into the treasury of Porto Rico, to be expended as required by law for the government and benefit thereof instead of being paid into the Treasury of the United States.

* * * * *

SEC. 14. That the statutory laws of the United States not locally inapplicable, except as hereinbefore or hereinafter otherwise provided, shall have the same force and effect in Porto Rico as in the United States, except the internal-revenue laws, which, in view of the provisions of section three, shall not have force and effect in Porto Rico.

* * * * *

Act of Mar. 2, 1917, ch. 145, 39 Stat. 951 *et seq.*:

* * * * *

SEC. 9. That the statutory laws of the United States not locally inapplicable, except as hereinbefore or hereinafter otherwise provided, shall have the same force and effect in Porto Rico as in the United States, except the internal-revenue laws: *Provided, however*, That hereafter all taxes collected under the internal-revenue laws of the United States on articles produced in Porto Rico and transported to the United States, or consumed in the island shall be covered into the treasury of Porto Rico.

* * * * *

SEC. 58. That all laws or parts of laws applicable to Porto Rico not in conflict with any of the provisions of this Act, including the laws

relating to tariffs, customs, and duties on importations into Porto Rico prescribed by the Act of Congress entitled "An Act temporarily to provide revenues and a civil government for Porto Rico, and for other purposes," approved April twelfth, nineteen hundred, are hereby continued in effect, and all laws and parts of laws inconsistent with the provisions of this Act are hereby repealed.

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No. 80-1252

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

COMMONWEALTH OF PUERTO RICO,
Petitioner,

v.

DONALD T. REGAN, SECRETARY
DEPARTMENT OF THE TREASURY,
Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit

PETITIONER'S REPLY TO RESPONDENT'S BRIEF IN OPPOSITION

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1. Respondent's lengthy brief in opposition is more important for what it does not say than for what it does. Respondent simply does not dispute the fact that this action is of exceptional importance to the United States of America, the Commonwealth of Puerto Rico, and the Virgin Islands. Nor could he in light of the representations made to the Court of Appeals in his suggestion for hearing *en banc*. *See* Petn. at 67a-72a. Instead, respondent spends twenty-four printed pages arguing that the decision below is correct. Yet, even respondent concedes

that the words of the statutory provision at issue "permit [the] reading, advanced by petitioner." Brief in Opposition ("Br. Opp.") 8. In light of that concession (and similar concessions made below) and the unquestioned national importance of the issues presented, the need for plenary review by this Court is indisputable.

2. In his brief in opposition, respondent advances numerous arguments in support of his contention that the decision below is correct. Certain of those arguments are so egregiously erroneous that a brief reply is necessary.

a. Respondent mischaracterizes petitioner's position by claiming that Puerto Rico seeks rebate of all taxes on any transaction involving articles produced in Puerto Rico and transported to the United States. Br. Opp. 8. Based on that mischaracterization, respondent attempts to conjure up a litany of horrors involving alleged administrative problems associated with petitioner's claim. *Id.* at 8-9. First, that effort demonstrates the extent to which respondent must go to avoid the facts of this case. Contrary to respondent's apparent wish, this case involves the gasoline excise tax, not a tax imposed upon the transportation of property by air. The Court need only consider the facts presented by the case before it; it need not consider theoretical cases existing only in the minds of advocates. Second, respondent's argument that, if petitioner prevails, taxes would have to be covered over to Puerto Rico whenever there is tax "on any transaction involving a Puerto Rican article", Br. Opp. 9, ignores the language of the cover over provision. That provision reaches only "taxes *collected . . . on articles* produced in Puerto Rico and transported to the United States." (Emphasis supplied.) Gift, estate, sales, or transportation taxes are not at issue here. What is at

issue is the gasoline excise tax, which clearly is imposed on the article. *See* 75 *Cong. Rec.* 11657 (1932) (remarks of Senator Walsh) ("The manufacturers' excise tax proposal [for gasoline] is to lev [sic] the tax once, *upon the article*, in its finished state. . . . ")(emphasis supplied).

b. Respondent asserts that petitioner's claim is refuted by the "complementary relationship" between 26 U.S.C. §7652(a)(3) and 26 U.S.C. §7652(a)(1). Br. Opp. 11. However, that assertion overlooks the unqualified admonition in the Internal Revenue Code that "[n]o inference, implication, or presumption of legislative construction shall be drawn or made by reason of the location or grouping of any particular section or provision or portion of this title. . . . " 26 U.S.C. §7806(b). Subsections (a)(1) and (a)(3) derive from two entirely different statutes, the Foraker Act of 1900, 31 Stat. 77, and the Jones Act of 1917, 39 Stat. 951, enacted for totally different purposes, seventeen years apart.

c. Respondent misrepresents the meaning of the legislative history when, in his effort to demonstrate that "the taxes to be covered over by this section were the Foraker Act equalization taxes," Br. Opp. 14, he uses ellipses in quoting the House Report. This is evident from the following:

The full quotation H.R. Rep. No 77, 64th Cong., 1st Sess. 1 (1916):	Respondent's revision Br. Opp. 14:
"It appears that the present rule is to pay *into the Porto Rican Treasury those taxes that are collected under the internal-revenue laws of the United States on articles produced and used in Porto Rico, and* into the Treasury of the United States internal-revenue taxes collected on articles produced in Porto Rico but transported to the United States." (Emphasis supplied for omitted portion.)	" the present rule is to pay..... .... into the Treasury of the United States internal-revenue taxes collected on articles produced in Porto Rico but transported to the United States."

Thus, the phrase "these taxes" referred not merely to equalizaton taxes imposed by the Foraker Act but also to taxes "on articles produced and used in Porto Rico," which *cannot* have been equalization taxes. The Senate amendment to the cover over provision made it diverge even more sharply from the Foraker taxing provision by including taxes on articles "produced elsewhere" (not just in the United States) but consumed in Puerto Rico. Petn. at 10.[1]

[1] Respondent's assertion, Br. Opp. 14, that there were no U.S. internal revenue taxes "relating to Puerto Rico other than the Foraker Act taxes" is irrelevant. The House and Senate reports make clear that the Congress was legislating a matter of principle — that any taxes which might *then or thereafter* be imposed on Puerto Rican articles or on articles of other manufacture consumed in Puerto Rico would be covered into the treasury of Puerto Rico.

d. *Griffin* v. *California,* 380 U.S. (1965), cited by respondent, Br. Opp. 16, is inapposite. Petitioner does not suggest that any adverse inference should be drawn from respondent's withholding, on grounds of privilege, of twenty-three concededly relevant documents. Petitioner argues that *no* inference should be drawn. The point is not whether respondent can invoke various privileges; it is that respondent should not be able to make an affirmative argument based on allegedly consistent administrative construction while withholding some such constructions for whatever reason. To allow respondent to claim a consistent course of administrative construction while withholding documents that would or may disprove that claim is akin to allowing a defendant to invoke the advice of counsel defense while, at the same time, making otherwise valid assertions of the attorney-client privilege. One cannot make affirmative use of an attorney's advice while refusing to permit inquiry into the nature of the advice. *United States* v. *Miller,* 600 F.2d 498 (5th Cir. 1979), *cert. denied,* 444 U.S. 955 (1980); *Hyde Construction Co.* v. *Koehring Co.,* 455 F.2d 337 (5th Cir. 1972); *Trans World Airlines, Inc.* v. *Hughes,* 332 F.2d 602 (2d Cir. 1964), *cert. dismissed,* 380 U.S. 248 (1965). Fairness precludes use of such advice as both a sword and a shield. The same principle of basic fairness is applicable here. Either respondent must produce all relevant documents or no inference concerning respondent's administrative construction should be drawn.

e. Respondent attempts to rebut petitioner's argument that the decision below allows certain gasoline to escape taxation by asserting that the broad definition of "producer" in 26 U.S.C. §4082(a) precludes the possibility that gasoline could go untaxed. Br. Opp. 20. The short answer is that respondent's assertion proves

too much. If firms that ship gasoline from Puerto Rico to the United States could be taxed as "producers" pursuant to section 4082(a), then so could firms that ship gasoline from any foreign country to the United States. Respondent's position thus would render the term "importer" in 26 U.S.C. §4081(a) redundant, contrary to the rule that all words in a statute should be given effect and should not be construed in a manner that would render them surplusage. *Administrator, FAA* v. *Robertson*, 422 U.S. 255, 261 (1975); *Wilderness Society* v. *Morton*, 479 F.2d 842, 856 (D.C. Cir.), *cert. denied*, 411 U.S. 917 (1973). The bankruptcy of respondent's argument is amply demonstrated by his final, wholly unsupported assertion that "importer" means one thing when used in sections 5001 and 5701 and yet another when used in section 4081(a). Br. Opp. 21-22.

f. Finally, respondent would have this Court believe that "the gasoline taxes claimed by petitioner had . . . been paid by the Secretary into the 'Highway Trust Fund,' the 'Land and Water Conservation Fund', and the 'Airport and Airway Trust Fund.' " Br. Opp. 22. That simply is not true. There is no earmarking or dedication of the gasoline tax receipts into the Highway Trust Fund or any other fund. Instead, Congress appropriated from general revenues *amounts equivalent to* stated percentages of various taxes collected under certain provisions of the Internal Revenue Code, *see, e.g.*, §209(c), Highway Revenue Act of 1956, 70 Stat. 387, 398, and even respondent has conceded below that the gasoline excise tax receipts are paid into the general fund of the United States Treasury. In short, as the District Court correctly concluded,[2] the statute "simply does not create the bar that [respondent] asserts it creates." Petn. at 55a.

[2] The Court of Appeals did not reach the issue.

CONCLUSION

For the reasons set forth above and in the petition, a writ of *certiorari* should issue to review the judgment and opinion of the United States Court of Appeals for the District of Columbia Circuit.

Respectfully submitted,

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April 17, 1981

Certificate Of Service

I, Michael J. Henke, attorney for petitioner and a member of the Bar of this Court, certify that on this 17th day of April, 1981, the foregoing Reply has been served upon respondent by hand-delivering three copies thereof to David English Carmack, Department of Justice, Washington, D.C., attorney for respondent and by mailing three copies, postage prepaid, to the Solicitor General, Department of Justice, Washington, D.C. 20530. I further certify that all parties required to be served have been served.

/s/ MICHAEL J. HENKE
Michael J. Henke